

PUBLIC HEARING
STATE OF CALIFORNIA
DEPARTMENT OF FOOD AND AGRICULTURE
DAIRY MARKETING BRANCH

HOLIDAY INN CAPITOL PLAZA
300 J STREET
CALIFORNIA ROOM
SACRAMENTO, CALIFORNIA

WEDNESDAY, AUGUST 4, 2004

9:00 A.M.

JAMES F. PETERS, CSR, RPR
CERTIFIED SHORTHAND REPORTER
LICENSE NUMBER 10063

PETERS SHORTHAND REPORTING CORPORATION (916) 362-2345

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Ms. Candace Gates, Research Manager I

Ms. Kristina Kreutzer, Milk Pooling Branch Auditor

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PROCEEDINGS

HEARING OFFICER ESTES: Good morning, everyone.

My name is Richard Estes. I'm the Hearing Officer today. We're going to be conducting this hearing today, on August 4th, 2004, at the Holiday Inn Capitol Plaza, 300 J Street, Sacramento, hear in the California Room.

And the hearing will begin now at approximately 9 a.m.

This hearing is being called pursuant to Article 7 & 8 Chapter 2 Part 3 Division 21 of the Food and Agricultural Code as implemented by Title 3, Section 2080.2 of the California Code of regulations.

The reason we're having this hearing today is because we received a petition from Clover Stornetta Farms on June 1st, 2004. And the petition regards proposed amendments to the transportation allowance system in the pooling plan.

Today's call of the hearing is for the purpose of considering the petitioner's proposal to amend the full plan in effect on August 4th, 2004, to amend transportation allowances from milk moving into Marin and Sonoma counties.

In addition, the hearing will consider proposals to amend the pooling plans and the stabilization plans in

1 effect on August 4th, 2004, to provide incentives to move
2 milk to higher usages. These include provisions for
3 transportation allowances, transportation credits, and the
4 milk movement requirements.

5 The hearing will also consider the factual basis
6 evidence and legal authority upon which to make any and
7 all proposed amendments to the plan.

8 As most of you I think are already aware if you
9 attended the pre-hearing workshop, we have received five
10 alternative petitions. And they are from California
11 Dairies, Incorporated; the Dairy Farmers of America,
12 Incorporated; the Dairy Institute; Security Milk Producers
13 Association -- and Security Milk Producers Association.
14 And we will take testimony from them in support of their
15 petition after we received the presentation from Clover
16 Stornetta.

17 Just so that everyone knows the procedure that
18 will be followed today: My name is Richard Estes, as I
19 said. I'm the hearing officer. I do not take any
20 substantive role in the hearing today. My purpose here is
21 solely to administer this hearing today and make sure that
22 everyone has an opportunity to present everything they
23 need to put into the record in support of their position
24 and to present their perspective to the Department about
25 the petition and the alternative petitions today.

1 The panel today that is off to my left consists
2 of Dr. Eric Erba, who's the Senior Agricultural Economist
3 of the Dairy Marketing Branch, who I also might note has
4 just been recently appointed to be a special assistant to
5 Animal Health, I believe. So we're very pleased and
6 congratulate him on that. Certainly hope to do well.

7 David Ikari, Branch Chief of the Dairy Marketing
8 Branch; Don Shippelhouse, Research Manager I of the Dairy
9 Marketing Branch; and John Lee, Branch Chief of the Milk
10 Pooling Branch.

11 In terms of if you want to testify today and you
12 are not one of the petitioners, please sign the witness
13 sign-in list in the back of the room. We will take
14 witnesses in the order in which they have signed the
15 sign-in list. And people in the back of the room to
16 assist you I believe are Kristina Kreutzer and Venetta
17 Reed. So please seek their assistance if you want to
18 testify today.

19 Also I believe they have a copy -- they have
20 copies of the hearing notice available for your perusal.
21 I don't know if they have copies of the petitions
22 themselves, but I believe they do.

23 I'm seeing that they do not. But they do have
24 the hearing notice.

25 In terms of the conduct of the hearing, please

1 speak directly to the call of the hearing to the greatest
2 extent possible.

3 This is a fairly substantive hearing in nature.
4 And please treat the panelists and other witnesses in the
5 public with respect. You know, character attacks,
6 innuendo, other types of rhetorical strategies that might
7 work in other context aren't especially useful here and
8 really don't get much consideration by the panel in my
9 view. So please keep that in mind as we proceed with the
10 hearing today.

11 The hearing reporter today is James Peters of
12 Peters Shorthand. We will have a transcript maintained
13 with the Department, if you want to come and review a
14 transcript of today's hearing. But it is maintained at
15 the Department. You will have to come to the Dairy
16 Marketing Branch to review that transcript. If you want
17 you're own transcript for your own purposes in
18 representing yourself or others, you will have to obtain
19 that from Peters Shorthand Corporation. And they are
20 located at 3336 Bradshaw Road, Suite 240, sacramento,
21 California 95827. Their phone number is 916-362-2345.

22 At this time, we will introduce the exhibits into
23 the record pertinent to the call of today's hearing. And
24 they will be introduced by Candace Gates.

25 And who's with you, Candace?

1 RESEARCH MANAGER I GATES: Kristina Kreutzer.

2 But she's going to actually enter today.

3 HEARING OFFICER ESTES: I see. All right.

4 So Kristina Kreutzer of the Department will be
5 introducing the exhibits today.

6 Ms. Kreutzer, do you swear or affirm to tell the
7 truth and nothing but the truth today?

8 MILK POOLING BRANCH AUDITOR KREUTZER: I do.

9 HEARING OFFICER ESTES: And what is your position
10 with the Department?

11 MILK POOLING BRANCH AUDITOR KREUTZER: I'm an
12 auditor with the Milk Pooling Branch.

13 HEARING OFFICER ESTES: All right. And you're
14 here today to introduce the exhibits in the record for
15 call of the hearing?

16 MILK POOLING BRANCH AUDITOR KREUTZER: Yes, I am.

17 HEARING OFFICER ESTES: And could you please
18 proceed to describe them for admission into the record.

19

20 MILK POOLING BRANCH AUDITOR KREUTZER: Okay. My
21 purpose here this morning is to introduce the Department's
22 composite hearing exhibits numbered 1 through 43.
23 Relative to these exhibits previous issues of Exhibits 9
24 through 43 are also hereby entered by reference.

25 The exhibits being entered today have been

1 available for review at the offices of the Dairy Marketing
2 Branch since the close of business on July 28th, 2004.

3 An abridged copy of the exhibits is available for
4 inspection at the back of the room. A copy of the exhibit
5 list is also available at the back of the room.

6 I ask at this time that the composite exhibits be
7 received.

8 HEARING OFFICER ESTES: All right. Please bring
9 them forward.

10 We will introduce Exhibits No. 1 through 43 into
11 the record at this time.

12 I am not going to read the list of these
13 exhibits, as they are -- an abridged list is available for
14 your review in the back of the room. And they will be
15 maintained as part of the permanent hearing record. So
16 I'm not going to read them and take the public's time in
17 going through that list.

18 But just to note that if you are curious as to
19 their content, you can review a list of them in the back
20 of the room. I think there's also an abridged collection
21 of them there. So if you have an interest in that, please
22 go to the back of the room so that we can avoid spending
23 the next 25 minutes reading the list, for those of you who
24 are probably pretty much aware of the their content.

25 So we'll introduce them into the record at this

1 time Exhibits No. 1 through 43.

2 (Thereupon the above-referred to documents
3 were marked, by the hearing officer,
4 as Exhibits 1-43.)

5 MILK POOLING BRANCH AUDITOR KREUTZER: Mr.
6 Hearing Officer, the exhibit next in order is a letter
7 dated August 4th, 2004, from Driftwood Dairy, James E.
8 Dolan.

9 Mr. Hearing Officer?

10 HEARING OFFICER ESTES: All right. That will be
11 Exhibit No. 44.

12 (Thereupon the above-referred to document
13 was marked, by the hearing officer, as
14 Exhibit 44.)

15 MILK POOLING BRANCH AUDITOR KREUTZER: Okay. Mr.
16 Hearing Officer, the exhibit next in order is a letter
17 dated August 4th, 2004, from Humboldt Creamery, Richard
18 Ghilarducci, President and CEO.

19 HEARING OFFICER ESTES: This will be Exhibit No.
20 45.

21 (Thereupon the above-referred to document
22 was marked, by the hearing officer, as
23 Exhibit 45.)

24 MILK POOLING BRANCH AUDITOR KREUTZER: Mr.
25 Hearing Officer, I ask for a period of time in which to

1 file a post-hearing brief.

2 HEARING OFFICER ESTES: Who's doing that? Is the
3 Department doing that or is it the -- Mr. Gillarducci's
4 doing that?

5 MILK POOLING BRANCH AUDITOR KREUTZER: The
6 Department.

7 HEARING OFFICER ESTES: Okay. The Department is
8 doing that. All right.

9 The request for a post-hearing brief is granted.
10 The Department shall have through --

11 MR. TILLISON: Mr. Hearing Officer, there are a
12 number of people --

13 HEARING OFFICER ESTES: State your name.

14 MR. TILLISON: My name is Jim Tillison, Alliance
15 of Western Milk Producers.

16 There are a number of people who are not here due
17 to vacations and so forth. And, therefore, I would
18 request that you grant a period of filing briefs of ten
19 working days. That would give us until Wednesday -- what
20 is it, August -- two weeks from today basically. So it
21 would be August 18th.

22 HEARING OFFICER ESTES: Okay. Well, first of all
23 let me address two things in regard to your request, Mr.
24 Tillison.

25 First of all, the ability to file a post-hearing

1 brief is dependent upon appearing at the hearing today and
2 providing testimony and then seeking clarification or
3 elaboration on your remarks or the remarks of others.

4 So the only people that will be -- that have the
5 legal ability to file a post-hearing brief is the
6 Department, because the Department is here obviously, and
7 yourself and others. And they are filed, like I said, for
8 the purpose of clarifying issues that are raised during
9 the course of the hearing today and not for the purpose of
10 presenting arguments.

11 So in that respect, individuals that testify
12 today may request the opportunity to submit post-hearing
13 briefs, or individuals who also present public comment;
14 distinguishing between, you know, people who testify in
15 support of their petitions and people who testify or
16 present as witnesses.

17 So in any event, I want to make that clear that
18 the only people that will be filing post-hearing briefs
19 will be people who are here today and providing some type
20 of public comment.

21 In terms of the time period. My inclination is
22 to have it -- have the post-hearing brief period go
23 through Friday, the 13th of August, unless that presents
24 some special hardship for anyone here today.

25 MR. TILLISON: Mr. Hearing Officer, as I said, it

1 does present a hardship. I am presenting testimony on
2 behalf of CDI. They are going to have to take it -- to
3 provide any specific questions that are asked. And the
4 main parties that would be involved in that won't be
5 available until after the 13th.

6 HEARING OFFICER ESTES: Okay. Well, I appreciate
7 you clarifying that for the record.

8 Okay. Then we will -- post-hearing briefs: The
9 Department is authorized to file a post-hearing brief.
10 The Department shall have the opportunity to file that
11 brief through Wednesday, August 18th, 2004, at 4:30 p.m.
12 Obviously the Department doesn't have to FAX or deliver
13 its brief to itself. If any other individual wishes to
14 file a post-hearing brief, I will address that request at
15 that time and give appropriate information as to the
16 delivery and the presentation of that brief to the
17 Department in a timely manner.

18 MILK POOLING BRANCH AUDITOR KREUTZER: Mr.
19 Hearing officer, this concludes my testimony.

20 HEARING OFFICER ESTES: All right. Would you
21 please bring those exhibits forward.

22 The letter dated August 4th, 2004, from Driftwood
23 Dairy as described by Ms. Kreutzer will be introduced into
24 the record as Exhibit No. 44.

25 And the letter from Humboldt Creamery by Mr.

1 Ghilarducci, dated August 4th, 2004, shall also be entered
2 into the record as Exhibit No. 45.

3 At this time we will proceed to take testimony in
4 support of the petition by Clover Stornetta Farms. So if
5 representative from Clover Stornetta would please come
6 forward.

7 Clover Stornetta shall have up to one hour to
8 present testimony in support of this petition today. So
9 we will commence with that testimony at this time.

10 Sir, I assume you're from -- if you would please
11 pass out copies of your testimony to myself and the panel.
12 And then we'll swear you into the -- swear you in, and
13 then you can proceed with your testimony.

14 Please sit at the witness table.

15 And let me swear you in. And if we have problems
16 with you being heard, the hearing reporter will let you
17 know.

18 Mr. Gary Imm; is that correct?

19 MR. IMM: Correct.

20 HEARING OFFICER ESTES: Do you swear or affirm to
21 tell truth and nothing but the truth today?

22 MR. IMM: I do.

23 HEARING OFFICER ESTES: And could you please
24 state your name and spell your last name for the record.

25 MR. IMM: My name is Gary Imm I-m-m.

1 HEARING OFFICER ESTES: And on whose behalf are
2 you testifying today?

3 MR. IMM: On behalf of Clover Stornetta Farms,
4 Inc.

5 HEARING OFFICER ESTES: And on what basis have
6 you been authorized by Clover Stornetta, Incorporated, to
7 appear on their behalf?

8 MR. IMM: I'm the CEO of Clover Stornetta Farms.

9 HEARING OFFICER ESTES: I see here that you have
10 presented a written text of your anticipated testimony
11 today?

12 MR. IMM: Yes.

13 HEARING OFFICER ESTES: And is it correct that --
14 would you like to have that introduced in the record?

15 MR. IMM: I would.

16 HEARING OFFICER ESTES: All right. We will
17 introduce the written text of your testimony as presented
18 into the record today as Exhibit No. 46.

19 (Thereupon the above-referred to document
20 was marked, by the hearing officer, as
21 Exhibit 46.)

22 HEARING OFFICER ESTES: And so please proceed.

23 MR. IMM: Thank you.

24 Mr. Hearing officer and members of the hearing
25 panel. My name is Gary Imm. I'm the Chief Executive

1 Officer of Clover Stornetta farms, Inc.

2 Clover Stornetta is a fluid milk processor and
3 distributor with one processing plant located in Petaluma,
4 California. We distribute product primarily in the
5 western portion of northern California, basically Monterey
6 north. We currently have 17 producers under contract who
7 ship to our Petaluma plant.

8 Clover Stornetta Farms, Inc., has requested a
9 change in the Milk Pooling Plan, Section 921.2 sub (a)
10 whereby Sonoma and Marin counties would be added to the
11 Bay Area receiving area. This testimony provides a broad
12 overview, specific information, and then a modified
13 proposal based upon information gathered to date,
14 including that presented at the Department's workshop on
15 July 20, 2004.

16 Our request seeks to redress the current inequity
17 created by our exclusion from transportation allowances.
18 As such, we will focus on the relative differences between
19 our local haul and a haul to the Bay Area receiving area.

20 Overview. The Bay Area continues to grow and
21 expand to the north. One result of this expansion is that
22 Marin and Sonoma counties have become a part of the Bay
23 Area for both the marketing and procurement of Class 1
24 milk.

25 There is far more producer milk delivered to

1 Class 1 and Class 2 plants outside of Sonoma and Marin
2 counties than there is delivered to Class 1 and Class 2
3 plants within Sonoma and Marin counties. This has created
4 a deficit situation for Sonoma and Marin counties' Class 1
5 pool.

6 Clover Stornetta Farms, Inc., contracted with our
7 own producers beginning in October of 1999. A review of
8 our negotiations and contracts with these producers shows
9 that one of the largest issues was transportation costs.
10 Our producers took pride in serving the fluid market, but
11 made it very clear to us that pride would not pay their
12 feed bills. We were required then, and continue today, to
13 equalize our producers' hauling costs with those of other
14 Sonoma and Marin producers who were and are shipping into
15 the Bay Area. At that time, in 1999, this extra cost was
16 determined to be 12 cents per hundredweight.

17 Hauling rates themselves seem to defy some basic
18 laws of economic common sense. Our experience is that
19 larger processors are extended hauling rates based on
20 total volume and some vague credit for receiving plant
21 capacities. We have evidence that haulers think in terms
22 of dollars per hour for shorter hauls and dollars per mile
23 for longer runs. This economic thought process tends to
24 increase the relative cost of shorter hauls and decrease
25 the relative cost of longer hauls.

1 The substantial volumes of milk from the North
2 Valley also lend themselves to reduced hauling to the
3 current Bay Area receiving area. We understand that at
4 least one hauler believes that after delivering a load
5 from the North Valley to the Bay Area, a load from Sonoma
6 or Marin County by the same truck can be considered a
7 "backhaul" and costed as such.

8 Finally, with respect to hauling differences,
9 there is a constantly changing dynamic between the fixed
10 and variable portion of the haul. For example, in times
11 of rapidly increasing fuel costs, one would expect to see
12 the variable portion of hauling increase in relationship
13 to the fixed. This would tend to increase the spread
14 between short and long hauls, but only for such time as
15 fuel costs were spiking.

16 Specifics. The Department publishes a survey of
17 hauling rates entitled "Hauling Rates, Ranch to Plant".
18 An average of these hauling rates from July 2000 through
19 August 2003 shows a local North Bay haul of 42.2 cents per
20 hundredweight and a Bay Area haul of 40.1 cents per
21 hundredweight. If these rates are correct, then Clover
22 Stornetta Farms is disadvantaged by .422 less .401, plus
23 the 24 cent transportation allowance, for a total of 26.1
24 cents per hundredweight.

25 The numbers for April 2004, which we were told

1 were actually May costs but April fluid pounds, show a
2 reversal from the average and a very dramatic reversal
3 from the previous study of August 2003. The April 2004
4 rates show the local haul decreasing by 7 mills per
5 hundredweight, to .443 per hundredweight, and the Bay Area
6 haul increasing by 9.7 cents per hundredweight to 49.3
7 cents. If these rates are correct, then Clover Stornetta
8 is disadvantaged by .443 less .493 plus the 24 cent
9 transportation allowance, for a total of 19 cents per
10 hundredweight.

11 We submitted our hauling costs to the Department
12 for April 2004. These costs for April, adjusted for the
13 May surcharge, show that Clover Stornetta Farms' May cost
14 was .4205 per hundredweight for our 17 contracted
15 producers.

16 While the .4205 per hundredweight is an accurate
17 total cost, we believe that in fairness to all producers a
18 part of this should be excluded. Clover Stornetta Farms
19 has organic producers in our producer group. The haul for
20 organic, because of its specialized timing and load sizes,
21 is more costly than conventional. Since we have made this
22 business decision, we do not believe the pool should be
23 asked to subsidize it in any way. Our hauling for May
24 2004 for our producers, excluding organic producers, was
25 38.9 cents per hundredweight.

1 Conclusion and proposal. We do not know why the
2 ranch-to-plant hauling rates show such a dramatic recent
3 change. We do believe that the relative difference
4 between the local and Bay Area hauls is more accurately
5 represented by the April 2004 numbers. All of the
6 anecdotal evidence that we have about other Class 1 and
7 Class 2 processors competing for producers in Marin and
8 Sonoma counties shows a Bay Area haul that is somewhere
9 between 5 to 8 cents per hundredweight higher than our
10 local rate.

11 If we use the Department's average rate for the
12 past three years, then our request to simply to be added
13 to the Bay Area is reasonable. If we use the hauling
14 rates that we believe to be correct, our proposal must be
15 modified to ask for something less.

16 We still believe that we belong in the Bay Area
17 receiving area. We are a part of the Bay Area by any
18 measure of our business.

19 We propose that a new bracket of zero to 40 miles
20 be added to the Bay Area receiving area. This bracket
21 would be indexed to 8 cents per hundredweight less than
22 whatever the rate is in the new 41 to 99 mile bracket.
23 Currently that rate would be 24 cents -- it would be the
24 24 cents that is now in the zero to 99 bracket, which
25 would make the zero to 40 mile bracket 16 cents per

1 hundredweight.

2 This proposal should have the effect of
3 equalizing costs, encouraging milk to move to the closer
4 Class 1 plant, minimizing the cost to producers, and
5 creating continuity in the greater Bay Area.

6 Thank you for giving us this opportunity to
7 testify. I do request the opportunity to submit a
8 post-hearing brief, and would be happy to try to answer
9 any questions that you might have.

10 Respectfully submitted, Gary Imm.

11 HEARING OFFICER ESTES: Mr. Imm, your request to
12 file a post-hearing brief is granted. As I said before,
13 the post-hearing brief should be filed with the
14 Department, or submitted -- delivered to the Department in
15 some form or another by August 18th, 2004, on Wednesday,
16 at 4:30 p.m.

17 I'm going to ask for the panel's assistance.

18 What is the address, given our building
19 situation?

20 DAIRY MARKETING BRANCH ACTING CHIEF ERBA: Still
21 1220.

22 HEARING OFFICER ESTES: Twelve twenty.

23 So please have it delivered to 1220 N street.

24 What's the suite number for that? Do we have a
25 suite number?

1 DAIRY MARKETING BRANCH ACTING CHIEF ERBA: No.

2 HEARING OFFICER ESTES: So we just have it
3 directed to the Dairy Marketing Branch?

4 DAIRY MARKETING BRANCH ACTING CHIEF ERBA: Right.

5 HEARING OFFICER ESTES: At 1220 N street,
6 Sacramento, California.

7 DAIRY MARKETING BRANCH ACTING CHIEF ERBA:
8 The Milk Pooling Branch.

9 HEARING OFFICER ESTES: So please direct your
10 post-hearing brief to the Dairy Marketing Branch or the
11 Milk Pooling Branch as we just discussed, 1220 N Street,
12 Sacramento, California 95814.

13 Also I think there is a -- you can fax your brief
14 to 916-341-6697, which is the fax number I have here for
15 the Dairy Marketing Branch.

16 MR. IMM: Thank you.

17 HEARING OFFICER ESTES: So do we have any panel
18 questions for Mr. Imm?

19 DAIRY MARKETING BRANCH ACTING CHIEF ERBA: I have
20 a couple questions.

21 Mr. Imm, do you have any processing facilities in
22 Marin County?

23 MR. IMM: We do not.

24 DAIRY MARKETING BRANCH ACTING CHIEF ERBA: Why
25 have you included Marin County in your proposal then?

1 MR. IMM: If we're going to make a definition of
2 the greater Bay Area, it did not make sense to skip Marin
3 County. And I know that there is a processor in Marin
4 County. It just didn't make sense to do that. But we
5 have no interest in Marin County.

6 DAIRY MARKETING BRANCH ACTING CHIEF ERBA: Have
7 you considered, instead of adding Sonoma and Marin
8 counties to the current Bay Area receiving area, instead
9 setting up your own separate receiving area, separate from
10 the Bay Area? I know you've made some arguments for why
11 you should be included in the Bay Area. But logistically
12 it might be easier to just set up a separate receiving
13 area entirely and deal with the Bay Area and whatever you
14 call the North Coast Bay Area separate pieces. Have you
15 considered that?

16 MR. IMM: We've considered it. We wouldn't have
17 any objection to doing that. It made sense for us to be
18 in the Bay Area. It is the greater Bay Area. But if that
19 is -- if that complicates the issue rather than
20 simplifying the issue -- and what we're looking for is
21 equity. And wherever that's best accomplished within the
22 Milk Pooling Branch, that's fine with us.

23 DAIRY MARKETING BRANCH ACTING CHIEF ERBA: I have
24 no further questions.

25 MILK POOLING RESEARCH MANAGER SHIPPELHOUTE: Mr.

1 Imm, you're looking for equity between yourselves and
2 other Class 1 bottling plants in the area -- or in Bay
3 Area. Thinking of the transportation allowance as it was
4 originally established, it was to encourage milk to move
5 from distant supply counties into deficit counties.

6 Do you believe there's more milk produced in your
7 county -- in Marin and Sonoma counties than there is
8 utilization, or do you think it's the opposite?

9 MR. IMM: I think within the greater Bay Area
10 it's the opposite. Sonoma and Marin County cannot supply
11 the greater Bay Area fluid market.

12 MILK POOLING RESEARCH MANAGER SHIPPELHOUTE: And
13 with the closing of the Petaluma -- the Dairy Farmers of
14 America cheese plant in Petaluma, does that change some of
15 the marketing conditions for you and some of the contract
16 negotiations for you?

17 MR. IMM: That will not change anything
18 specifically for us because we have our own producers.
19 But that's -- an interesting variable that's been thrown
20 in since we gave our petition. And it has caused milk --
21 additional milk movement out of our county into other
22 fluid plants. I don't know -- we've been watching this
23 since 1999, so we are taking rather the historical basis
24 here, which is consistent with everything we've said and
25 us being disadvantaged. And I don't know how to address

1 that plant closing. I do know that -- I understand that
2 the person who -- we've been told has that plant in escrow
3 has every plan to reopen that as a cheese plant.

4 So that's an issue that has yet to be fully
5 resolved as to how that will impact the milk supply long
6 term in the North Bay.

7 MILK POOLING RESEARCH MANAGER SHIPPELHOUTE: No
8 further questions.

9 DAIRY MARKETING BRANCH CHIEF IKARI: I just have
10 a couple.

11 Mr. Imm, the Dairy Institute's proposal would
12 implement a 15 cent allowance for zero to 99. And yours
13 is 16. Give you an opportunity to address why the 16
14 versus the 15. Is there any data or evidence you can
15 share with us on why one is better than the other?

16 MR. IMM: There really is not. As I look through
17 the Department's historical data and I looked through our
18 data, and I -- and I can only tell you that most of the
19 information we have about competing rates is we are -- we
20 don't have ability to get those documents. We are -- I
21 can only tell you what we are told out there.

22 So I think -- we're within pennies. If anybody's
23 testimony is within pennies, based on the information that
24 any individual has, we are all substantively correct in
25 our assumptions.

1 DAIRY MARKETING BRANCH CHIEF IKARI: Would you
2 care to comment or provide testimony with respect to the
3 proposal of CDI with respect to the Bay Area receiving
4 and, in particular, in Sonoma and Marin counties.

5 MR. IMM: The only observation I would make there
6 is that they're testifying to a higher rate that has
7 happened because of that plant closure which is -- which I
8 think is very consistent with what I was talking about as
9 far as when we do go out and try to get hauling rates, the
10 other factors that transportation companies throw into the
11 mix, the synergies that they can enjoy or not enjoy, the
12 long-term relationships and the viability of a long-term
13 contract for that milk. I don't know how the higher rate
14 on some loads coming out -- I don't even know how the
15 Department blends that rate with the existing rates. I do
16 know -- or think that I know that for at least one of the
17 major Class 1 procurers of milk is -- County there's at
18 least two years left on a hauling contract. So I do not
19 expect to see those higher rates implemented soon with
20 other Class 1 purchasers in our area.

21 DAIRY MARKETING BRANCH CHIEF IKARI: Thank you.

22 MILK POOLING BRANCH CHIEF LEE: Gary, would you
23 explain -- in your testimony you mentioned about the
24 organic -- hauling for organic -- because of the
25 specialized timing, load sizes. And why is it more costly

1 than conventional?

2 MR. IMM: Basically the main reason is that we
3 often can't get full tankers. You may -- because of the
4 very nature of it, you may make a run out and come back
5 with 2,000 gallons. The fixed costs -- the variable costs
6 are the same; you just divide them by smaller loads
7 typically.

8 MILK POOLING BRANCH CHIEF LEE: Also, too,
9 concerns about hauling costs as such. Are you seeing from
10 the producers they're not willing to sell you milk? Is
11 there any indication of that because of their ability not
12 to get an additional transgression allowance currently?

13 MR. IMM: I'm not sure how to answer that. We
14 have 17 dedicated producers. But I can only give you this
15 answer, which probably doesn't give you exactly the answer
16 that you're looking for: But in our industry it's very
17 important for us to have a relationship with those
18 producers. So there might be producers out there who
19 would be willing to sell us milk for less than the ones
20 that we have now. And we wouldn't know that because we
21 wouldn't solicit that, because we have a relationship and
22 we have an agreement and we have a contract with 17
23 producers.

24 MILK POOLING BRANCH CHIEF LEE: But at this point
25 there hasn't been any discussion that they will change

1 their method of how much milk they'll be willing to sell
2 to you because of the current situation of the
3 transportation?

4 MR. IMM: None at all, no.

5 MILK POOLING BRANCH CHIEF LEE: Thank you.

6 DAIRY MARKETING BRANCH ACTING CHIEF ERBA: I have
7 one follow-up question for you, Gary.

8 You made some adjustments to your original
9 proposal when you through in that shorter mile bracket,
10 the zero to 40 mile bracket. How did you arrive at zero
11 to 40 mile bracket? Previously there was a zero to 99
12 bracket. How did you draw the line at 40 miles? Or why
13 did you draw the line at 40 miles?

14 MR. IMM: That's a great question. And it was
15 relatively arbitrary. I thought that I had seen some zero
16 to 40 mile brackets in other schedules. I did want to --
17 I was trying to separate -- include us in the Bay Area but
18 separate us from affecting the current Bay Area rate. And
19 I believe that going no more than 40 miles, that would
20 never impact any milk that is now currently going from
21 Sonoma and Marin counties into the Bay Area.

22 DAIRY MARKETING BRANCH ACTING CHIEF ERBA: Is
23 there any milk coming into your plant going more than 40
24 miles?

25 MR. IMM: There's one load coming in more than 40

1 miles.

2 DAIRY MARKETING BRANCH ACTING CHIEF ERBA: Okay.

3 And just to be clear -- I think I understand, but I want
4 to be clear on this. You've taken in with the zero to 40
5 mile bracket, and then you start the brackets already
6 there, now the zero to 99, you'd start that at 40.1 miles
7 and go to 99?

8 MR. IMM: That's my proposal, yes.

9 DAIRY MARKETING BRANCH ACTING CHIEF ERBA: Okay.
10 Thank you.

11 HEARING OFFICER ESTES: Okay. Do we have any
12 additional questions for Mr. Imm?

13 All right. Seeing none --

14 MILK POOLING RESEARCH MANAGER SHIPPELHOUTE: Yes.

15 Mr. Imm, looking at some of the mileage brackets
16 on other schedules, I see zero to 44 for the Solano
17 receiving area. Your county is neighboring to Solano. Is
18 there any reason you distinguished yourself with Bay Area
19 rather than Solano? Or associated yourself, I should say.

20 MR. IMM: That has to do, in my mind, because
21 there are Class 1 processors coming up and contracting
22 directly with producers in our marketing area, along with
23 some co-op milk that's going out there.

24 So in Sonoma and Marin -- even though there is
25 some milk going into Solano from our area, the vast

1 majority of it does go to the Bay Area. And that is
2 also -- or one of them is leaving Sonoma and Marin County
3 and going into the Bay Area with larger quantities than we
4 contract for. And, quite frankly, our competition from
5 those pool plants is coming back out of the Bay Area into
6 our area.

7 So we just consider ourselves a part of that
8 greater Bay Area.

9 MILK POOLING RESEARCH MANAGER SHIPPELHOUTE: So
10 most of the marketing conditions then -- package product
11 marketing as well as competition for the raw product?

12 MR. IMM: Competition for the producers is much
13 more intense from the fluid processors in the Bay Area,
14 yes.

15 MILK POOLING RESEARCH MANAGER SHIPPELHOUTE:

16 Okay. And you were -- you're indicating that you
17 wanted to address some equity issues. Could those equity
18 issues be addressed by disallowing milk coming out of the
19 Sonoma and Marin County moving into the Bay Area? That's
20 for receiving transportation allowance going into some of
21 those Bay Area plants that currently get the
22 transportation allowance.

23 MR. IMM: I guess a quick answer to that would
24 be, I suppose it could be if the resulting milk that was
25 all coming into -- if the resulting vacuum that was filled

1 by that not happening of milk coming into other fluid
2 processors in the Bay Area arrived at a rate after
3 transportation allowance that was not less than our rate
4 without the transportation allowance, if that makes sense.
5 So you change one dynamic for another. If that created
6 equity, that is all that we're looking for, we'd have to
7 expand then the idea of equity to all of northern
8 California and other transportation allowances. We'd have
9 to address those at the same time. But if we could get
10 equity by reducing levels other places across the board,
11 we have no problem with that. We're just looking for
12 equity.

13 MILK POOLING RESEARCH MANAGER SHIPPELHOUTE:

14 Thank you.

15 MR. IMM: Thank you.

16 HEARING OFFICER ESTES: All right. Do we have
17 any more questions?

18 All right. Thank you for your testimony today.

19 MR. IMM: Thank you.

20 HEARING OFFICER ESTES: We're going to take the
21 alternative petitions in order here momentarily. I just
22 want to note Dr. Erba, who apparently can also fill in
23 with the Legal Office on an emergency basis, I guess, has
24 drawn to my attention to Food and Agriculture Code Section
25 61903, which states that the period of time for

1 post-hearing briefs is not to exceed ten calendar days.
2 So I read that to be, we cannot permit the filing of a
3 post-hearing brief after Tuesday, August 17th.

4 The statute says not to exceed ten calendar days
5 following the close of date of public hearing. So the
6 first day would be tomorrow, given that today is the
7 closing of the hearing.

8 So the Department's post-hearing brief should be
9 concluded -- or prepared by August 18th -- August 17th,
10 Tuesday, 4:30 p.m.; and also, Mr. Imm, your brief as well
11 should be presented on Tuesday by 4:30 and not Wednesday
12 by 4:30.

13 And we'll state the same thing for the record
14 whenever additional requests for post-hearing briefs.

15 MILK POOLING RESEARCH MANAGER SHIPPELHOUTE: And
16 what's the date?

17 HEARING OFFICER ESTES: Tuesday, the 17th.

18 MILK POOLING RESEARCH MANAGER SHIPPELHOUTE:

19 That's puts us --

20 DAIRY MARKETING BRANCH ACTING CHIEF ERBA: No,
21 no, that's not right.

22 HEARING OFFICER ESTES: That's not even right, is
23 it?

24 Okay. Well, today is the 4th. So basically it
25 will have to be -- Saturday is the 14th. So I believe

1 that permits us to go through Monday, being that's a
2 holiday. That's what was considered a non-business day at
3 least for court purposes. So I'm going to interpret the
4 statute as giving us ten days through August 14th. For
5 filing court records, for example, you get to the next day
6 open for business, which is the -- which in this instance
7 would be the 16th.

8 So let me repeat that again and try to eliminate
9 all the confusion that's just been created.

10 (Laughter.)

11 HEARING OFFICER ESTES: All post-hearing briefs
12 should be submitted to the Department by the close of
13 business on Monday, August 16th at 4:30 p.m. You can mail
14 or hand deliver your brief to the Department by the 16th
15 at 1220 N Street, Sacramento, California 95814. And make
16 that to the attention of either the Milk Pooling Branch or
17 Dairy Marketing Branch. You can also fax that brief to
18 the Department, 916-341-6697, again by 4:30 p.m., Monday,
19 August 16th.

20 So hopefully, Mr. Tillison, you can work with
21 that with your -- unfortunately we're restricted by
22 statute. So we'll have to proceed on that basis.

23 We will now proceed to take testimony in support
24 of the petitions -- the alternative petitions. And we
25 will take -- before anyone comes forward, let me just say

1 that we will take testimony in the following order in
2 support of these petitions:

3 First we will take -- first will be California
4 Dairies, Incorporated; second shall be Dairy Farmers of
5 America, Incorporated; thirdly shall be Dairy Institute;
6 fourth will be Land O' Lakes; and fifth will be the
7 Security Milk Producers Association. Each shall be given
8 30 minutes to testify in support of their alternative
9 petitions.

10 So unless there's any objection to that order of
11 presentation, we will now proceed to take testimony from
12 California Dairies, Incorporated.

13 Mr. Tillison, do you swear or affirm to tell the
14 truth and nothing but the truth?

15 MR. TILLISON: I do.

16 HEARING OFFICER ESTES: And would you please
17 state your name and spell your last name for the hearing
18 reporter.

19 MR. TILLISON: My name is James Tillison T, as in
20 Tom, i-l-l-i-s-o-n. I'm the Executive Vice President and
21 CEO of the Alliance of Western Milk Producers.

22 HEARING OFFICER ESTES: On whose behalf -- I see
23 that you're presenting the alternative positions for
24 California Dairies, Incorporated. Could you please
25 describe on what basis you're appearing on their behalf

1 today?

2 MR. TILLISON: Yes. They are a member of the
3 Alliance, and I was asked to appear on their behalf.
4 Their position and their testimony was approved by their
5 board of directors, as was my representing their
6 organization. I am not here testifying on behalf of the
7 Alliance. I am hear testifying on behalf of California
8 Dairies, Incorporated.

9 HEARING OFFICER ESTES: I see that you've given
10 out a written statement that I assume will conform to your
11 testimony today.

12 MR. TILLISON: Yes.

13 HEARING OFFICER ESTES: And would you like to
14 have that introduced into the record?

15 MR. TILLISON: Yes.

16 HEARING OFFICER ESTES: It will be introduced
17 into the record as Exhibit No. 47.

18 (Thereupon the above-referred to document
19 was marked by the hearing officer as
20 Exhibit 47.)

21 HEARING OFFICER ESTES: So please proceed with
22 your testimony today.

23 MR. TILLISON: Thank you.

24 Unfortunately I can't make disparaging remarks.
25 But the 17th will work for us because some of us do work

1 on the 16th.

2 Mr. Hearing Officer and members of the panel. My
3 name is Jim Tillison, Executive Vice President and CEO of
4 the Alliance of Western Milk Producers. This testimony
5 today will be on behalf of the California dairies
6 incorporated, CDI, a milk marketing cooperative
7 representing approximately 700 producers marketing over 40
8 percent of the milk produced in California.

9 The recommended changes CDI proposes was approved
10 by their board of directors on June 22nd and again on July
11 27th of 2004.

12 The call of this hearing to consider milk
13 movement incentives within the Pooling Plan for market
14 milk and the Stabilization and Marketing Plans for market
15 milk is timely because of increased hauling costs and
16 changes in the movement of milk to Class 1 markets.

17 CDI contractually supplies one fluid processor in
18 the Bay Area, Alameda County, and is the major provider of
19 fluid milk to fluid processors in the southern California
20 area. This testimony will specifically address the milk
21 movement costs to those markets and will be consistent in
22 one underlining objective: That producers should be
23 responsible for local hauls. Milk movement incentives
24 should be structured to compensate producers for
25 additional costs over local hauling costs in providing

1 fluid milk to fluid customers through transportation
2 allowances. That's ranch-to-plant movement. Incentives
3 should be from the closest available production area,
4 thereby discouraging milk movement from distant locations.
5 Transportation credits, plant-to-plant, should also be
6 established to encourage movement of milk from local
7 plants and incorporate disincentives from distant
8 locations to minimize the cost to the producer pool in
9 California.

10 Therefore, CDI recommends the following changes
11 only to the Pooling Plan for market milk:

12 Section 921.2:

13 For plants located in the Bay Area receiving
14 area, which shall consist of the counties of Alameda and
15 Contra Costa:

16 For milk shipments from Marin and Sonoma, from
17 zero through 99 miles, 34.75 cents per hundredweight; for
18 milk shipments from all other areas, from zero through 99
19 miles, 25 cents per hundredweight, over 99 miles, 29 cents
20 per hundredweight.

21 Plants in southern California receiving area,
22 which shall consist of the counties of Los Angeles,
23 Orange, Riverside, and Ventura:

24 For milk shipments from Santa Barbara, San Diego,
25 Imperial, Kern, Kings, and Tulare counties, from zero

1 through 89 miles, 10 cents per hundredweight; over 89
2 miles through 139 miles, 47.75 cents per hundredweight;
3 and over 139 miles, 61.75 cents per hundredweight.

4 For milk shipments from all other areas, from
5 zero through 89 miles, 10 cents per hundredweight; over 89
6 miles, 20 cents per hundredweight.

7 For plants located in the San Diego receiving
8 area, which shall consist of San Diego County:

9 For milk shipments from zero through 89 miles, 10
10 cents her hundredweight.

11 Justification and supporting documentation for
12 the above-suggested changes are as follows:

13 1) CDI has reduced the Bay Area receiving areas
14 to only Alameda and Contra Costa counties because to their
15 knowledge the other Bay Area counties do not need milk
16 movement incentives. CDI's milk shipments from Marin and
17 Sonoma counties to Alameda County have a 60 cent per
18 hundredweight hauling cost (Five J's Trucking, which is
19 attached and labeled Exhibit A). CDI experiences a local
20 producer hauling rate of 25.2 cents per hundredweight for
21 the majority of their members in the central and northern
22 California. And, therefore, this request for milk
23 shipments from Marin and Sonoma counties is the difference
24 of 34.75 cents per hundredweight. Shipments from other
25 areas is an increase of 1 cent per hundredweight over

1 current allowances to cover diesel fuel increases.

2 Since this recommendation excludes a local haul
3 cost, CDI would oppose Clover Stornetta's request for
4 Marin and Sonoma counties to be added in receiving
5 allowances. Most of their members are within 30 miles of
6 the Clover Stornetta plant, and the local haul rate of
7 25.25 cents per hundredweight incorporated into CDI's
8 proposal should be more than adequate to cover hauling
9 costs of that short distance. Clover Stornetta does not
10 seem to have difficulty in obtaining milk at competitive
11 prices or retaining their independent producers because of
12 higher hauling costs.

13 2) Unlike the Bay Area, CDI is very
14 acknowledgeable and highly involved in milk movement
15 patterns in southern California. The requested increases
16 in the two highest mileage zones in the Los Angeles,
17 Orange, Riverside, and Ventura counties are actual hauling
18 costs from independent third party hauler (Kings County
19 Truck Lines, Exhibit B) less the local haul rate.

20 For example, Bakersfield area, which is Kern
21 County, 73 cents per hundredweight. Local haul rate,
22 25.25 cents per hundredweight. Requested for 90 to 139
23 miles, 47.75 per hundredweight.

24 McFarland area rate, which is also in Kern
25 County, 87 cents per hundredweight. Local rate, 25.25

1 cents per hundredweight. Request over 139 miles, 61.75
2 percent per hundredweight.

3 Also listed on Exhibit B is the rate from Kern
4 County -- from north of Kern County which CDI is not
5 recommending full coverage. The maximum allowable
6 transportation allowance should be 61.75 cents per
7 hundredweight for the over 139 mile bracket, which will
8 discourage or build in a disincentive of approximately 7
9 cents per hundredweight for any milk movement from Tulare
10 County. There is adequate milk in Kern County to supply
11 with fluid milk requirements of southern California over
12 and above the local milk in the southern California area.

13 CDI's supportive of the recommended change by
14 Land O' Lakes to split the southern California receiving
15 area into two receiving areas getting different
16 allowances. They are, however, recommending different
17 rates with milk shipments from Santa Barbara, San Diego,
18 Imperial, Kern, Kings, and Tulare counties receiving the
19 higher rates justified above, and all other shipments from
20 other counties to receive a lower rate.

21 This lower rate over 89 miles compensates the
22 shipments from Barstow/High Desert area into Los Angeles,
23 which has a rate of 54 cents per hundredweight as to CDI's
24 projected rate of 34 cents per hundredweight into a local
25 manufacturing plant in San Bernardino. The difference is

1 how CDI arrives at the 20 cent per hundredweight allowance
2 over 89 miles. Milk currently does not move into a local
3 manufacturing plant from that area, so an actual hauling
4 cost is not available.

5 It cannot be overemphasized enough the importance
6 of adequate transportation allowances from Kern County tea
7 to Los Angeles area fluid handlers. During the past 12
8 months CDI has lost over 20 percent of their milk
9 production in southern California, which amounts to over
10 1.5 million pounds each day, and continual decreases are
11 expected resulting in more and more milk from Kern County
12 will have to move to southern California.

13 3) The last suggested change is an increase of 1
14 cent per hundredweight in the San Diego area for zero
15 through 89 miles, similar to the other areas in southern
16 California for hauling increases due to labor and diesel
17 fuel.

18 CDI is also recommending to drop the mileage
19 bracket of over 89 miles because milk does not and will
20 not move to San Diego County over 89 miles since there is
21 only one fluid processor in that area.

22 4) It is CDI's understanding that the alternative
23 proposals submitted by Dairy Farmers of America
24 incorporates a local haul deduction from recommended rates
25 for plants in Solano County and, therefore, CDI is

1 supportive of their request.

2 In regards to transportation credits, CDI
3 recommends the following changes only to the Stabilization
4 and Marketing Plans for market milk:

5 Section 300.2. Designated supply county, los
6 Angeles County; minimum deduction per hundredweight, 38
7 cents; designated deficit counties, Los Angeles or Orange
8 counties.

9 Los Angeles County; minimum deduction per
10 hundredweight, 48 cents; for Riverside, San Diego, or
11 Ventura counties.

12 The above changes reflect new labor and diesel
13 fuel costs for plant-to-plant deliveries from Los Angeles
14 County. They have segregated the designated deficit
15 counties from the designated supply county of Los Angeles
16 into two groupings to allow for plants in Los Angeles
17 county to be competitive with the plant-to-plant movement
18 from outlying areas. CDI is currently disadvantaged in
19 the condensed sales deliveries from their Artesia plant in
20 southern California as compared to plants over 200 miles
21 from Los Angeles.

22 The above requested changes are identical to
23 CDI's submitted alternative proposal. But at their Board
24 of Directors meeting held on July 27, 2004, the Board
25 passed a motion to continue to be strongly opposed to

1 transportation credits on condensed skim milk which was
2 added at the last transportation hearing. As previously
3 stated, CDI's local plant in Artesia is disadvantaged as
4 to condensed sales; and if a decision from this hearing is
5 made to remove transportation credits for condensed skim,
6 CDI will withdraw their request for Los Angeles to Los
7 Angeles movement because they then would have a
8 competitive position on those sales.

9 In either event, however, it is vital that a new
10 higher rate be allowed from Los Angeles to Riverside, San
11 Diego and Ventura counties (see Kings County Truck Lines,
12 Exhibit C attached), which will allow CDI to recover their
13 freight costs on plant-to-plant sales to those longer
14 distant areas. This request in transportation credits
15 will simply allow their local Los Angeles plant an equal
16 competitive position for sales opportunities without being
17 burdened with freight costs that are being subsidized for
18 others.

19 Similar to CDI's request on transportation
20 allowances, they do support cost-related adjustments to
21 transportation credits from others today as long as some
22 shortfall exists from distant locations to encourage
23 plant-to-plant movement from closer locations. This
24 position is consistent with CDI's past testimony at
25 previous hearings addressing transportation credits.

1 CDI would like to thank you for this opportunity
2 to submit their recommended changes and would like to
3 request a post-hearing period for CDI to answer or clarify
4 any questions regarding this testimony.

5 That concludes their testimony.

6 HEARING OFFICER ESTES: Your request for a
7 post-hearing brief is granted. Please have that either
8 delivered or fax'd to the Department by close of business
9 Monday, August 16th, at 4:30 p.m.

10 MR. TILLISON: Thank you.

11 HEARING OFFICER ESTES: At this time we will --
12 at this time are there panel questions for Mr. Tillison?

13 MILK POOLING RESEARCH MANAGER SHIPPELHOUTE: Mr.
14 Tillison --

15 MR. TILLISON: Yes.

16 MILK POOLING RESEARCH MANAGER SHIPPELHOUTE: You
17 indicated that it does not seem to CDI that Clover has
18 difficulty obtaining milk for their plant.

19 MR. TILLISON: Yes, sir.

20 MILK POOLING RESEARCH MANAGER SHIPPELHOUTE: Do
21 you know that or is that something you're assuming?

22 MR. TILLISON: I believe that the people writing
23 the testimony are aware of the situation. They said they
24 believed that Clover did not have any producers outside 30
25 miles. Their testimony today indicated that they only had

1 one producer outside of 40 miles. So I would assume using
2 their local haul logic, that that's how they arrived at
3 the proposal or the request to deny the Clover Stornetta
4 request.

5 MILK POOLING RESEARCH MANAGER SHIPPELHOUTE: But
6 you don't know if Clover has had -- is having to subsidize
7 some of those hauling charges to equalize with producers
8 that are getting transportation allowance into the Bay
9 Area currently?

10 MR. TILLISON: I believe all they know is what
11 they heard at the post-hearing workshop, which was a total
12 cost situation. In talking with Mr. Korsmeier, however,
13 his feeling was that what they were paying for hauling
14 costs was greater than CDI has been able to obtain from a
15 different trucker in that same area. So they believe
16 that -- frankly they believe that Clover Stornetta is not
17 in a favorable position in terms of their hauling
18 contract.

19 MILK POOLING RESEARCH MANAGER SHIPPELHOUTE: And
20 you also testified that you had a projected rate on the
21 milk in southern California. This projected rate, what
22 kind of a time period were you projecting that rate, or
23 were you --

24 MR. TILLISON: Well, I can have them answer that
25 question specifically. I believe the rate they're using

1 is based on a quotation that they received from Kings
2 County Trucking, which I believe is attached, less what
3 they believe is the local haul.

4 MILK POOLING RESEARCH MANAGER SHIPPELHOUTE: So
5 that's not a rate that's projected out? They're trying to
6 estimate what the cost is historically.

7 MR. TILLISON: It's based on the information
8 provided to them from Kings County Trucking as to what
9 they are or will be charging.

10 MILK POOLING RESEARCH MANAGER SHIPPELHOUTE:
11 Regarding the condensed sales, the Artesia plant.
12 You indicate that you are currently disadvantaged to
13 plants that are much further away from the receiving
14 plants than the Artesia plant is.

15 Is that disadvantage a result of the current
16 operation of the pool plan or the stabilization plan?

17 MR. TILLISON: Yeah, they believe that the
18 disadvantage was created, as in the testimony presented,
19 at the last hearing when there was an adjustment made to
20 the condensed situation. As they say in their testimony,
21 CDI's basic belief is that there not be a transportation
22 allowance -- or credit rather -- I'm sorry -- paid on
23 condensed shipments.

24 MILK POOLING RESEARCH MANAGER SHIPPELHOUTE: So
25 eliminating that would give, as you testified, CDI a

1 competitive position in those sales?

2 MR. TILLISON: Yes.

3 MILK POOLING RESEARCH MANAGER SHIPPELHOUTE:

4 Would that competitive position be enhanced by
5 the transportation allowance received by milk pooling into
6 Artesia?

7 MR. TILLISON: That's a -- you know, that's an
8 interesting question. I think that in my discussions with
9 Mr. Korsmeier, he would simply state that, you know,
10 that's the way things are, that there is a transportation
11 credit into their plant; and it is what it is, is the way
12 he put it to me when I asked the same question.

13 MILK POOLING RESEARCH MANAGER SHIPPELHOUTE: So,
14 wouldn't your -- or CDI's competition probably answer the
15 same way if asked about transportation credits for
16 condensed skim?

17 MR. TILLISON: Well, I think that what it goes
18 back to is the basic premise I believe that's involved in
19 both transportation allowances and should be involved in
20 transportation credits and, that is, that the closest skim
21 milk should go to where it's needed.

22 I believe the CDI has more than adequate capacity
23 to provide the condensed needs of the plants in southern
24 California.

25 MILK POOLING RESEARCH MANAGER SHIPPELHOUTE: If

1 we were to eliminate the transportation credit on that
2 condensed skim, and that milk still received
3 transportation allowance, then the argument could be made
4 that the competitive position that CDI would enjoy was a
5 result of the consideration of the stabilization plan or
6 the pooling plan?

7 MR. TILLISON: I guess one could make that -- you
8 know, make that conclusion. I think that southern
9 California is a state -- is a deficit area in terms of
10 milk available for Class 1 and Class 2 uses. And that
11 situation is only going to be exacerbated, meaning that,
12 as they state in their testimony, more milk is going to
13 have to move into southern California for those uses.

14 So, therefore, you know, one could argue the milk
15 wouldn't move unless there was a transportation allowance,
16 meaning that that market would have a shortfall in milk
17 available. However, as far as transportation credits are
18 concerned, I believe CDI's argument is that they can
19 provide the milk on a local basis with the supply that's
20 available. It's the old "How much milk is in the bucket?"
21 Do you take all the milk from southern California and
22 condense it or sell it or do you put the milk that comes
23 in and mix it all altogether and some goes to fluid plants
24 and some goes to condensed?

25 MILK POOLING RESEARCH MANAGER SHIPPELHOUTE: You

1 indicate that CDI supports cost-related adjustment so long
2 as some shortfall exists from distant locations to
3 encourage plant-to-plant movement for closer locations.

4 What about ranch-to-plant movements? Is it the
5 same philosophy there as far as allowance rates from
6 distant plants?

7 MR. TILLISON: I think that they follow the
8 same -- I think that they follow the same philosophy. And
9 that what they're basically doing is taking an actual cost
10 and then reducing it for a local haul. How much milk
11 moves from above 139 miles in the southern market, I'm not
12 aware of. But I think that -- I don't think it's very
13 much. I think most of the movement is in the -- coming
14 from the Kern County area and not from Tulare County
15 above.

16 MILK POOLING RESEARCH MANAGER SHIPPELHOUTE: From
17 a policy standpoint -- as you point out there is less and
18 less milk being produced in southern California. And all
19 indications are that that's going to continue, and that
20 there is going to continue to be a need for that milk in
21 bottling plants in southern California.

22 So from a policy standpoint, why would we
23 differentiate between milk coming over from over 139 miles
24 from one county versus another so long as that milk is
25 serving a Class 1 plant?

1 MR. TILLISON: Well, because I believe that Mr.
2 Korsmeier feels and CDI feels that there is and will be
3 adequate milk supplies in Kern County to provide milk to
4 the southern California market. In fact, he mentioned to
5 me that when that milk is Kern County is not needed in
6 southern California, they in fact have the misfortune of
7 having to haul it up to Tipton, which is just south of
8 Tulare, to process into butter or powder. So their
9 feeling is is that there's adequate milk in Kern County
10 and there will be even more milk available in Kern County.
11 And I think to a certain extent that is supported by what
12 we've seen in terms of new dairies being constructed.
13 Most of the construction that we've seen of any
14 significant size dairies has been in the Kern County or
15 Kings County area.

16 MILK POOLING RESEARCH MANAGER SHIPPELHOUTE: No
17 further questions.

18 DAIRY MARKETING BRANCH ACTING CHIEF ERBA: I have
19 a couple questions for you, Mr. Tillison.

20 MR. TILLISON: Couldn't leave before this
21 hearing.

22 DAIRY MARKETING BRANCH ACTING CHIEF ERBA: You
23 stated in your testimony actually several times, primarily
24 in the 1st page, that milk from distant locations ought to
25 be discouraged. And what I'd like to get clarified is if

1 that milk is served at the market, then does it matter
2 where it comes from?

3 MR. TILLISON: I guess the question is is it
4 serving a market in place of milk that otherwise could
5 serve the market from a closer area?

6 DAIRY MARKETING BRANCH ACTING CHIEF ERBA: So
7 you're saying it's more of a displacement issue?

8 MR. TILLISON: Yes.

9 DAIRY MARKETING BRANCH ACTING CHIEF ERBA: Okay.

10 MR. TILLISON: I think that's where they're
11 coming from.

12 DAIRY MARKETING BRANCH ACTING CHIEF ERBA: Okay.
13 Also on the 1st page you make mention of the fact of a
14 cost minimization to the pool. And the panel in making
15 its recommendations in the past has been aware of, maybe
16 too aware of minimizing costs. How much emphasis needs to
17 be placed on minimizing costs to the pool for either
18 transportation credits or transportation allowances? Is
19 it something to be considered primarily or to think about
20 it and do the right thing anyway?

21 MR. TILLISON: Well, I think when they talk about
22 minimizing costs to the pool, their -- it's consistent
23 with their philosophy that you want the closest milk to
24 the market to move to the market. And, therefore, there
25 should not be incentives created so that closer milk is

1 bypassed, because, frankly, it's a better deal to haul
2 milk a distance.

3 I think as the witness from Clover Stornetta
4 said, closer-in hauls tend to be looked at on an hourly
5 basis, whereas the distance hauls fall on a mileage basis.
6 So there's a fairly significant difference in the cost per
7 hundredweight when you're hauling about 40 miles versus
8 when you're hauling it 139 miles.

9 DAIRY MARKETING BRANCH ACTING CHIEF ERBA: Well,
10 from a strict cost minimization point of view we'd
11 probably not do anything. That would minimize costs,
12 right?

13 MR. TILLISON: Well, that would minimize costs.
14 But I think you'd then have to look at the reason you have
15 transportation cost allowances and you have transportation
16 credits, and that's to get milk to move out of the butter
17 powder and out of the cheese plants to fluid markets. So
18 I think that -- I think the first concern has to be: Is
19 enough milk moving to the market at the lowest possible
20 cost, is the way -- I don't think you would separate the
21 two.

22 DAIRY MARKETING BRANCH ACTING CHIEF ERBA: Right.
23 I'm going to move on to a different topic.

24 Mr. Shippelhoute asked you already something
25 about the idea of using different rates for different

1 counties, so I won't go into that. What I'd like to make
2 sure I understand is how CDI developed the rates that
3 appear on page 2.

4 My understanding is that they used the rates they
5 were quoted from the trucking companies and subtracted out
6 their 25-25 rate that they developed from the producers in
7 the Central Valley, California. Is that universally true
8 for those rates?

9 MR. TILLISON: I believe that that is universally
10 true for the rates from the standpoint that in all cases
11 what they did is took the cost provided to them by their
12 hauler and deducted whatever the local haul was in a given
13 area. I think if you looked at the situation from the
14 Barstow area, for example, they're using a 34 cent rate
15 for the local haul, which is what they've been quoted,
16 versus the 25.25 cents. But I think their basic
17 philosophy is -- in looking at these adjustment is, number
18 1, what's the actual cost, and then, number 2, what's the
19 local hauler? Did they use the 25.25 in place of a local
20 hauler if one does not exist?

21 MR. TILLISON: That I can't answer. I believe
22 that they're using the 25.25 local haul in all instances.

23 DAIRY MARKETING BRANCH ACTING CHIEF ERBA: For
24 all of them. Okay.

25 MR. TILLISON: The adjustment that I think

1 probably the only place where that may not be the case --
2 and I'll ask them to confirm this in post-hearing brief --
3 is in the adjustment from 9 cents to 10 cents in the local
4 rate. As they say in there, that's basically been
5 increased to cover diesel and labor costs.

6 DAIRY MARKETING BRANCH ACTING CHIEF ERBA: Right.

7 On page 5 of your testimony you say specifically,
8 several times actually, that Kern County ought to be
9 serving Los Angeles. I'm just curious why would you pick
10 Kern County specifically when there are other large
11 dairy-producing counties right nearby. Is it the South
12 Valley that we're concerned about or just specifically
13 Kern County? Why should Kern County be favored over, say,
14 Tulare or Kings County?

15 MR. TILLISON: Well, I think that Kern County
16 simply because it's closer to the market than Tulare is.

17 As far as Kings County is concerned, probably
18 more milk in Kern County than there is in Kings County.
19 And there's a very likely possibility that there are more
20 CDI shippers in Kern County than in Kings County.

21 DAIRY MARKETING BRANCH ACTING CHIEF ERBA: Okay.

22 In the transportation hearing we had last year,
23 we were concerned -- the panel was concerned about milk
24 that would pick up both transportation allowances into a
25 plant and then also receive transportation credit moving

1 out as condensed. It seems like that was pretty minimal
2 last year. It also seems like with CDI's proposal to
3 include L.A. County as a deficit county and also a L.A.
4 County as a designated supply county, that that would
5 increase that opportunity greatly. Can you speak to that?

6 MR TILLISON: I really can't. I'm not that
7 knowledgeable as to what specifically their analysis of
8 that situation was. I think basically though you have to
9 go back to the vote that their board took on July 27th.
10 And that was, there shouldn't be transportation credits on
11 condensed milk.

12 DAIRY MARKETING BRANCH ACTING CHIEF ERBA: Okay.
13 I understand.

14 I have no more questions. Thank you.

15 DAIRY MARKETING BRANCH CHIEF IKARI: I do have
16 one question.

17 Philosophically, in reaching decisions on
18 transportation allowance and credits, there's a certain
19 amount of judgment. How can the Department -- why should
20 the Department be concerned about the disadvantage of
21 condensed -- you know, CDI's position of condensed skim
22 and not be concerned about the Clover Stornetta's
23 disadvantage relative to the other Bay Area processors?

24 MR. TILLISON: Well, I think that CDI, in my
25 discussions with the management there, are basically -- is

1 familiar with the milk haulers in that area. And they
2 basically believe that Clover Stornetta is paying too much
3 for hauling. And, therefore, that has created more of a
4 disadvantage than the transportation allowance is.

5 You know, I guess the question is: Should the
6 Department protect people from their inability to -- or
7 their lack of getting into favorable contracts. I mean at
8 some point it's the business's responsibility to live
9 within it's means. And as I said, I think CDI due to
10 their familiarity with the trucking firms in that area
11 believe that Clover Stornetta is getting less than a
12 favorable rate.

13 I think the other issue is that, as their CEO
14 testified to, they've got 17 producers, they're not
15 looking for any more producers, they haven't lost any
16 producers. So that's an indication to me that perhaps the
17 competitive concerns that they have don't exist.

18 DAIRY MARKETING BRANCH CHIEF IKARI: Does CDI
19 have any data that the Department can look at, examine,
20 review, that goes to the rate -- why 17 producers or their
21 size or their location, why the cost that they're paying
22 in terms of hauling might be inappropriate?

23 MR. TILLISON: Well, I believe that in their
24 testimony there is attached a quotation from the Five J's,
25 I believe, as to what the hauling cost is. And I believe

1 these people operate also --

2 DAIRY MARKETING BRANCH CHIEF IKARI: Is that on a
3 statewide basis or are we just talking about a local area?

4 MR. TILLISON: Well, you're talking about --
5 basically talking about a local area, the North Bay area.

6 DAIRY MARKETING BRANCH CHIEF IKARI: Okay.

7 MR. TILLISON: You know, hauling rates vary
8 across the state, I assume just as the cost of milk in
9 grocery stores --

10 DAIRY MARKETING BRANCH CHIEF IKARI: Okay.

11 MR. TILLISON: -- varies across the state.

12 But I can ask them if they can provide specific
13 information on that conclusion.

14 DAIRY MARKETING BRANCH CHIEF IKARI: Thank you.

15 HEARING OFFICER ESTES: Any additional questions
16 for Mr. Tillison?

17 MILK POOLING RESEARCH MANAGER SHIPPELHOUTE:
18 Yeah, the Five J's Trucking exhibit that you have attached
19 here, is that assuming that -- let me back up. Does Five
20 J's haul other milk for CDI?

21 MR. TILLISON: What do you mean other milk for
22 CDI?

23 MILK POOLING RESEARCH MANAGER SHIPPELHOUTE: Milk
24 in other areas other than North Bay?

25 MR. TILLISON: Well, this quotation specifically

1 covers North Bay. And I don't have any personal knowledge
2 in that's the only place that they haul milk. But looking
3 at the quotation, it would indicate to me that that in
4 fact is what they're doing, is they basically do operate
5 in the North Bay area, because their quotation is to haul
6 milk from petaluma/Point Reyes into San Leandro, into
7 Modesto, and into Los Banos.

8 MILK POOLING RESEARCH MANAGER SHIPPELHOUTE: The
9 reason for my question is, if I remember Clover's
10 testimony correctly, they indicated that some of the
11 hauling rates that other firms are able to receive are
12 based in part on business that a trucking company does
13 outside of the North Bay as well. So it's perhaps a
14 different marketing environment or different contractual
15 arrangement than CDI with Five J's. I'm just curious if
16 this quotation would stand at this price if the only milk
17 that Five J's hauls for CDI was from North Bay to North
18 Bay. Perhaps you could have Mr. Korsmeier comment on
19 that.

20 DAIRY MARKETING BRANCH CHIEF IKARI: Well, it
21 would be interesting to know whether or not this is a new
22 area, a new territory for Five J's or if they're already
23 hauling milk in that area and they're established. And
24 if, so how long?

25 MILK POOLING RESEARCH MANAGER SHIPPELHOUTE: And

1 a final question.

2 MR. TILLISON: Wait a minute.

3 MILK POOLING RESEARCH MANAGER SHIPPELHOUTE:

4 Okay.

5 MR. TILLISON: Okay.

6 MILK POOLING RESEARCH MANAGER SHIPPELHOUTE: CDI

7 has producers in the North Bay area obviously.

8 What customers does CDI have in the North Bay?

9 MR. TILLISON: Well, they don't have customers in
10 the North Bay. But they were moving some of that milk
11 into the DFA Petaluma facility for primarily balancing
12 purposes and so forth. Where that milk goes otherwise, I
13 can't tell you. Based on the quote, I would assume that
14 that milk is moving down to Turlock and possibly as far as
15 Los Banos.

16 MILK POOLING RESEARCH MANAGER SHIPPELHOUTE: So
17 then perhaps the closest market for that milk currently is
18 bottling plants in the Bay Area?

19 MR. TILLISON: Possibly.

20 MILK POOLING RESEARCH MANAGER SHIPPELHOUTE: And
21 if that's the case, should that milk continue to receive
22 transportation allowance?

23 MR. TILLISON: If it's the closest milk, yes.

24 MILK POOLING RESEARCH MANAGER SHIPPELHOUTE: All
25 right.

1 HEARING OFFICER ESTES: Have any additional
2 questions?

3 All right. Thank you for your testimony today,
4 Mr. Tillison.

5 MR. TILLISON: I'll be right back. I'm testify
6 for DFA also.

7 (Laughter.)

8 HEARING OFFICER ESTES: All right. So our next
9 alternative petition is Dairy Farmers of America. And
10 after having gone through a costume change, Jim Tillison's
11 back on their behalf.

12 Before Mr. Tillison commences his testimony, I
13 did just want to note for those of you who are here today
14 that Jim Aynes, who's a recently -- recent attorney for
15 the Department is here today. He's sitting off to the
16 right there. And he's a recently hired counsel to the
17 department. And there's a possibility he may be
18 conducting some of these hearings in the future. So that
19 you might be familiar with him, we introduced him today.
20 SO we're happy to have him. And hopefully he's happy to
21 be working with us as well. So you might look forward to
22 seeing him here in the future.

23 Mr. Tillison, I'm not going to swear you again
24 since you've already been sworn for the record. But I
25 do -- let me just ask you a couple of questions since

1 you're appearing on behalf of Dairy Farmers of America.

2 Could you please describe the basis by which
3 you're appearing on their behalf today.

4 MR. TILLISON: Dairy Farmers of America Western
5 Area Council is also a member of the Alliance of Western
6 Milk Producers. And as such, they asked me if I would
7 appear on behalf of DFA in place of Mr. Stueve, who's not
8 able to be here and present their written testimony.

9 HEARING OFFICER ESTES: Okay. I've handed out a
10 copy of his anticipated testimony that you're going to be
11 delivering today. Would you like to have that introduced
12 into the record?

13 MR. TILLISON: Please.

14 HEARING OFFICER ESTES: It will be introduced
15 into the record as Exhibit No. 48.

16 (Thereupon the above-referred to document
17 was marked, by the hearing officer, as
18 Exhibit 48.)

19 HEARING OFFICER ESTES: So please proceed.

20 MR. TILLISON: Mr. Hearing officer and members of
21 the hearing panel. My name is not Gary Stueve. My name
22 is Jim Tillison, Executive Director/CEO of the Alliance of
23 Western Milk Producers, appearing on behalf of Dairy
24 Farmers of America Western Area Council. They currently
25 manage and market the milk of their own cooperative

1 members as well as the milk of 72 independent producers
2 through dairy marketing services. Their testimony was
3 approved by Western Area Council Board of Directors at a
4 meeting held on July 20th, and they appreciate the
5 opportunity regarding -- to provide commentary regarding
6 milk movement incentives.

7 Our alternative proposal very specifically
8 involves only moderate upward adjustments of the
9 transportation allowance rates for Solano County. Our
10 justification for these modest changes reflect both the
11 actual cost increases and net costs incurred by DFA and a
12 comparison and adjustment to actual local delivery costs.

13 If you look at the submitted document entitled
14 "Solano County Transportation costs and comparisons to
15 local hauls" you'll see the actual costs of delivering
16 milk to Solano County. Copies of actual freight bills or
17 other documents from our primary haulers support these
18 numbers. Our request for an increase is based on the
19 difference between the actual costs of delivering to
20 Solano county versus actual local hauls as best as we
21 could determine.

22 In the table you will note that these costs
23 differences reflect the difference between local hauls
24 available to DFA and the actual costs of delivering milk
25 to Solano County. Contributing to the situation are

1 freight rate increases experienced in this past year of
2 approximately 7 cents per hundredweight versus one year
3 ago. These increases are specific to fuel costs
4 increases, workers' compensation increases and the
5 increased cost of serving urbanized areas.

6 Due to the relative lack of milk production in
7 Solano County and the need to attract milk to the county,
8 DFA is advocating no shortfall.

9 In addition to their request for changes to
10 Solano County receiving area, they would also like to
11 briefly offer their commentary on some of the other
12 proposals.

13 Clover Stornetta proposal: Regarding the
14 original petitioner's proposal, DFA opposes amending
15 Section 921.2 of the Milk Pooling Plan by the addition of
16 Marin and Sonoma counties to the Bay Area receiving area.

17 It is DFA's contention that the need for
18 transportation incentives in this area does not exist. It
19 is our belief that Clover does not have a problem
20 attracting milk to their plant; there exists an ample
21 supply of local milk.

22 Clover may counter and suggest that they've
23 developed and balance their own unique supply, so the pool
24 should pay them to -- pay them local freight. Our answer
25 would be that they have developed a highly specialized

1 milk supply as part of their marketing plan and the cost
2 of maintaining the specialized milk supply should rest
3 with the beneficiary of the marketing plan, that is,
4 Clover Stornetta.

5 DFA also adds that on at least two occasions
6 since late 2001 DFA has offered to deliver a part or all
7 of the Clover supply at competitive prices with our local
8 milk supply. This service would also include balancing
9 and local delivery.

10 Sonoma and Marin counties offer an ample milk
11 supply for local deliveries. Offering local
12 transportation incentives from milk delivered to Sonoma
13 and Marin counties would be similar to offering allowances
14 for local deliveries in Tulare and Stanislaus counties.
15 These incentives are simply not necessary.

16 CDI alternative proposal: DFA would like to
17 offer their support of the DFA proposal as it is written
18 for both northern California and southern California as it
19 relates to transportation allowances. In the past year in
20 southern California DFA has experienced an increase of
21 approximately 3 cents for the zero to 89 mile bracket; 6
22 cents for the 89 to 139 mile bracket; and 15 cent
23 increases for the over 139 mile bracket. It is especially
24 important that transportation allowances stay current due
25 to the growing need for southern California to import milk

1 from other areas as the migration of dairies out of
2 southern California escalates.

3 Like CDI, we've experienced increases in the cost
4 of supplying Alameda County. Our costs for deliveries to
5 Alameda County are higher for milk originating from Sonoma
6 and Marin counties versus nearby San Joaquin valley
7 counties. This is due to the increased costs of
8 assembling milk from smaller dairies and transporting this
9 milk through and delivering to a highly urbanized area.

10

11 We are not prepared -- DFA is not prepared to
12 offer a position on changes to transportation credits.

13 This concludes our testimony. Thank you for the
14 opportunity to testify. And DFA would like to request the
15 opportunity to file a post-hearing brief.

16 HEARING OFFICER ESTES: Your request is granted.
17 And please present it to the Department in a manner as we
18 previously discussed.

19 Do we have any questions for Mr. Tillison?

20 DAIRY MARKETING BRANCH CHIEF IKARI: I just have
21 one question.

22 In the testimony, one can assume, but I'd rather
23 not assume -- what is DFA's position with respect to the
24 Dairy Institute's proposal with respect to the North Bay
25 Area?

1 MR. TILLISON: They will have to respond that in
2 brief.

3 MILK POOLING RESEARCH MANAGER SHIPPELHOUTE:

4 Mr. Tillison, in DFA's testimony you make mention
5 of a specialized milk supply. Could you define what you
6 mean by specialized?

7 MR. TILLISON: Yeah. I believe Clover Stornetta
8 has made the business decision to require their shippers
9 to provide them with a higher quality milk and lower
10 somatic cell count. And I'm not familiar with their
11 specifics in terms what they do offer, but they use this
12 as a marketing tool for their milk.

13 So not unlike organic milk, I assume that there
14 are some producers who are willing to meet those
15 requirements and others who may be nearby that aren't
16 willing to meet those requirements.

17 So I believe that DFA feels that there's only
18 modest differences between their organic supply and the
19 specialized supply from their other resources.

20 MILK POOLING RESEARCH MANAGER SHIPPELHOUTE: No
21 further questions.

22 DAIRY MARKETING BRANCH ACTING CHIEF ERBA:

23 One question, Mr. Tillison.

24 Does the idea that there should be no shortfall
25 in the rates that have been proposed seem to be at odds

1 with previous testimony we've heard today?

2 MR. TILLISON: It would seem to be.

3 DAIRY MARKETING BRANCH ACTING CHIEF ERBA: Could
4 you ask DFA to justify why there should be no shortfall,
5 particularly with the longer distance hauls under that
6 Solano receiving area.

7 Thank you.

8 HEARING OFFICER ESTES: No additional questions?

9 Thank you for your testimony today.

10 MR. TILLISON: I won't be back.

11 HEARING OFFICER ESTES: Oh, you're not going to
12 be representing the Dairy Institute as well?

13 (Laughter.)

14 MR. TILLISON: I don't believe so.

15 HEARING OFFICER ESTES: Maybe you and Mr. Schiek
16 can kind of divide up all the petitioners amongst
17 yourselves.

18 We will next proceed to address the alternative
19 petition of the Dairy Institute.

20 And so you swear or affirm to tell the truth and
21 nothing but the truth today?

22 DR. SCHIEK: I do.

23 HEARING OFFICER ESTES: Could you please state
24 your name and spell your last name for the record.

25 DR. SCHIEK: Yes, it's William Schiek, that's S,

1 as in super, c-h-i-e-k.

2 (Laughter.)

3 DAIRY MARKETING BRANCH ACTING CHIEF ERBA: That's
4 sure different.

5 (Laughter.)

6 HEARING OFFICER ESTES: And it's always kind of
7 interesting whether it's humility or exaggeration is the
8 best way of being persuasive with the panel.

9 (Laughter.)

10 HEARING OFFICER ESTES: Dr. Schiek, could you
11 please describe how you've been authorized to speak on
12 behalf of the Dairy Institute today.

13 DR. SCHIEK: Yes, I was authorized by Dairy
14 Institute's Board of Directors. And they authorized me to
15 testify on their behalf.

16 HEARING OFFICER ESTES: I see.

17 And you've also given us a written statement of
18 your anticipated testimony. I assume you'd like to have
19 that introduced into the record?

20 DR. SCHIEK: I would.

21 HEARING OFFICER ESTES: That will be introduced
22 into the record as Exhibit No. 49.

23 (Thereupon the above-referred to document
24 was marked by the hearing officer as
25 Exhibit 49.)

1 HEARING OFFICER ESTES: And so please start to
2 commence with your testimony.

3 DR. SCHIEK: Okay. Mr. Hearing Officer and
4 members of the hearing panel. My name is William Schiek
5 and I'm an economist for the Dairy Institute of
6 California. And I am testifying on the Institute's
7 behalf.

8 The Dairy Institute is a trade association
9 representing 40 dairy companies which process
10 approximately 75 percent of the fluid milk, cultured and
11 frozen dairy products and over 60 percent of the cheese
12 products and a small percentage of the butter powder and
13 nonfat milk powder processed and manufactured in the
14 state.

15 Member firms operate in both marketing areas in
16 the state. And the position presented at this hearing was
17 unanimously adopted by Dairy Institute's Board of
18 Directors.

19 The Dairy Institute appreciates the opportunity
20 to testify today and to comment on the proposals by Land
21 O' Lakes, California Dairies, Inc., Dairy Farmers of
22 America, Security Milk producers, and Clover Stornetta
23 Farms, which are under consideration at this hearing. We
24 commend the Secretary for his willingness to consider
25 updating the regulatory framework in which our members

1 operate to make it reflective of current market
2 conditions.

3 We appreciate the excellent work and tremendous
4 effort put forth by the Department's staff in preparation
5 for this and other hearings. We all benefit from that
6 data and the analysis that the Department provides as it
7 helps us to make better-informed decisions regarding the
8 policies we propose.

9 At issue in this hearing are proposed changes to
10 the milk movement incentives contained in the Pooling Plan
11 and the Stabilization and Marketing Plan.

12 The broad purposes of milk movement programs have
13 been identified as follows: First, to assure an adequate
14 supply of milk to plants which provide Class 1 and Class 2
15 usage products to consumers; and, second, to assure that
16 higher usages have priority in terms of milk movement
17 incentives to producers; and, third, to encourage the most
18 efficient movement of milk to fluid usage plants.

19 Background: The enactment of milk pooling in
20 1969 fundamentally altered the relationships between Class
21 1 and processors and suppliers. Prior to pooling the
22 higher plant blend price that was paid by Class 1 plants
23 provided a positive incentive to attract milk to the
24 highest use. During the discussions leading up to the
25 Gonsalves Milk Pooling Act, producer representatives in

1 exchange for processor support made a commitment to ensure
2 that Class 1 plants would be served. From the beginning
3 it was recognized that fluid plants by virtue of the
4 higher minimum prices they pay, should be able to procure
5 necessary milk supplies without having to subsidize the
6 haul cost to their plants.

7 The current system of transportation allowances
8 and credits in California developed after a period where
9 milk movement incentives were limited primarily to area
10 differentials and location differentials on quota milk, a
11 system which is somewhat similar to the location
12 differentials employed in federal orders. Over time the
13 consolidation of marketing areas, growth in milk
14 production, and changing production and distribution
15 patterns and unique California geography necessitated new
16 milk movement mechanisms.

17 The transportation credits and allowances both
18 came into being in the early 1980's. The general
19 principle behind transportation allowances was that they
20 should compensate dairymen for the difference between a
21 local haul to a manufacturing plant and the longer haul to
22 the more distant fluid milk plant in a metropolitan area.
23 In the absence of such incentives producers would have an
24 incentive to ship their milk to a manufacturing plant and
25 a disincentive to serve the fluid milk market. When the

1 transportation allowance fully compensates producers for
2 the difference between a local haul and a long haul to a
3 fluid plant, the producer will be indifferent as to where
4 he ships his milk.

5 With respect to transportation credits, the
6 principle was to compensate the milk supplier for the cost
7 of shipping milk from a supplying plant to a deficit-area
8 plant after accounting for any difference in the marketing
9 area Class 1 differentials.

10 Historically, the transportation credits and
11 allowances have been set at levels that do not fully
12 compensate handlers for their shipment costs. A shortfall
13 in hauling compensation with respect to more distant milk
14 was supported by Dairy Institute in the past based upon
15 the assumption that it would encourage more efficient milk
16 movements.

17 The extent of the shortfall needed to encourage
18 orderly movement has been and continues to be a subject of
19 debate. And I will discuss in more detail later we
20 believe the application of the shortfall concept should
21 not be imposed to the extent that it creates a
22 disincentive for some plants to procure California milk
23 for Class 1 purposes.

24 We continue to believe that a milk movement
25 incentive system is necessary in order to meet the

1 statutory mandates and guidelines governing our industry.
2 In recent years the industry has continued to evolve and
3 has undergone considerable structural change.
4 Consolidation of supplying cooperatives and fluid milk
5 processors has changed the milk production and
6 distribution patterns. It is therefore appropriate to
7 review the existing system of transportation allowances
8 and credits to determine if changes are necessary.

9 One notion that has been troubling to Dairy
10 Institute's membership has been the belief expressed by
11 some in the industry that over-order premiums be relied
12 upon as a primary means to attract milk for fluid
13 purposes. We believe that it is consistent with the
14 purposes of milk stabilization and with the commitments
15 made by producer leadership at the inception of milk
16 pooling that milk should be attracted to Class 1 plants at
17 order prices.

18 Unfortunately, some in the producer community
19 have held the incorrect view that the sole purpose of the
20 Class 1 price differential is to enhance producer income,
21 instead of recognizing that in part the differential was
22 designed to assure that Class 1 markets are served.

23 We continue to maintain that the existing order
24 prices paid by processors provide more than enough revenue
25 to attract milk for Class 1 and mandatory Class 2

1 purposes, and that the marketing and pooling plans should
2 provide milk movement incentive mechanisms which are
3 adequate to ensure that those uses are served.

4 Dairy Institute's proposal and general concerns:
5 Dairy Institute believes that transportation allowances
6 and credits must be adequate to encourage milk to move
7 into higher use plants in deficit areas. When rates are
8 not adequate either the supplier or the customer gets
9 stuck with the transportation bill.

10 Milk suppliers and processing plants operate in a
11 competitive environment. Suppliers can attempt to absorb
12 the unrecovered transportation costs in the short run, but
13 in the longer run they must either pass those costs on or
14 stop supplying the Class 1 market.

15 If they choose to pass the costs on to the
16 processor, the higher use plant then must decide whether
17 to accept the higher cost or look for other sources of
18 milk.

19 If all processors are facing the same regulated
20 price and all suppliers are attempting to pass on the
21 unrecovered transportation costs, processors might elect
22 to subsidize the transportation of milk to their plants to
23 and pay the higher costs.

24 However, when processors face unequal regulated
25 milk prices relative to their competitors, as is in the

1 case in southern California, with exempt
2 producer-distributors and unregulated out-of-state
3 bottling plants, processors might attempt to find less
4 expensive milk supplies such as those located outside the
5 state.

6 Hence, inadequate transportation allowance and
7 credit rates can lead to Class 1 markets being served by
8 out-of-state suppliers to the detriment of the California
9 pool. Inadequate rates also lead to California Class 1
10 processors being both unable to compete favorably with
11 manufacturing plants for milk supplies. And they've got a
12 competitive disadvantage with respect to out-of-state
13 processors.

14 In order to secure the local Class 1 market for
15 California producers, transportation allowances and
16 credits must be adequate to draw milk without
17 transportation subsidization by a buyer or the supplying
18 cooperative.

19 Transportation allowances: Dairy Institute
20 continues to support the principle that transportation
21 allowance rates should be set equal to the difference
22 between the cost of the local haul and the cost of the
23 haul to higher use plants in metropolitan markets. The
24 transportation allowance system was meant to address the
25 narrow problem of how to attract milk to fluid plants in

1 metropolitan areas at order prices.

2 However, when setting allowance and credit rates,
3 equity among competing Class 1 plants in attracting milk
4 supplies is something that needs to be considered. This
5 is particularly true when the application of milk movement
6 incentives confers advantages on some Class 1 plants over
7 others. If these advantages would not have existed in the
8 absence of milk movement incentives, then the incentives
9 should adjusted to both 1) redress the inequitable impacts
10 and 2) ensure that fluid plants are adequately served.

11 With the foregoing in mind, Dairy Institute's
12 specific position is that fluid milk plants operating
13 within a market should not be disadvantaged relative to
14 each other in the procurement of nearby milk supplies. In
15 particular, the petitioner's proposal identifies a problem
16 where producers in Sonoma and Marin counties appear to
17 incur a higher net cost in shipping to the closest fluid
18 plant than they do in shipping their milk to more distant
19 markets in the Bay Area counties.

20 The apparent incentive that producers in Sonoma
21 and Marin counties have to bypass the closest fluid milk
22 plants and ship to more distant plants is due to the
23 application of the current transportation allowance race.
24 Current rates appear to give an advantage to Bay Area
25 plants with respect to the Sonoma and Marin milk supply.

1 It is our view that the North Bay, consisting of
2 Sonoma and Marin counties, the Solano receiving area, and
3 the Bay Area receiving area are each a part of a greater
4 San Francisco Bay Area market, which constitutes the
5 largest deficit fluid milk market in northern California.
6 Sonoma, Marin and Solano counties are located somewhat
7 closer to milk supplies than are many of the other in the
8 greater Bay Area and, as such, the incentives that are
9 required to move milk into plants in these counties may be
10 different than what is needed to move milk deep into the
11 Bay Area.

12 However, it is our view that plants in these
13 areas, which compete against each other within the greater
14 Bay Area market and which draw a portion of their milk
15 supply from Sonoma and Marin counties, should not be
16 disadvantaged with respect to each other in procuring
17 those supplies. Transportation allowances should,
18 therefore, be granted to producers shipping to fluid milk
19 plants located in Sonoma and Marin counties, as they are
20 in other plants in the Bay Area or Solano receiving areas,
21 if such allowances are needed to address competitive
22 concerns.

23 The allowance rates for producers from Sonoma and
24 Marin counties that ship to plants in the greater Bay Area
25 market -- I'm sorry, I'm repeating myself. The allowance

1 rates for producers from Sonoma and Marin counties that
2 ship to plants in the greater Bay Area market should be
3 adjusted so that the net hauling cost to Sonoma-Marin
4 producers is virtually identical regardless of whether
5 they ship their milk to a fluid plant in Sonoma and Marin
6 counties, Solano County, or Bay Area receiving area
7 counties. In order that milk moves in the most efficient
8 manner, it would not be inappropriate for the milk to have
9 a small incentive to move to closer to the closest fluid
10 milk plant.

11 We have changed the specific numbers in our
12 proposal to account for new information regarding hauling
13 rates while conforming to the principles described above.
14 We had fashioned our original alternative proposal using
15 the most recent hauling cost data available to us from
16 CDFA sources at the time alternative proposals were due.
17 In so doing we had to make some assumptions regarding the
18 cost of hauling milk from Sonoma and Marin counties to
19 Solano County, as that hauling cost was not published by
20 CDFA.

21 In view of the information that we had at the
22 time and the assumptions that we made, we earlier proposed
23 that producers shipping to eligible plants in Sonoma and
24 Marin counties, a newly designated North Bay receiving
25 area, receive a transportation allowance equal to 20 cents

1 per hundredweight. In order to equalize the competitive
2 situation with respect to this milk supply, we also
3 proposed that the transportation allowance for producers
4 in Sonoma and Marin counties who ship to the Bay Area
5 receiving area be reduced by 9 cents so that the new
6 transportation allowance of such shipments would have been
7 equal to 15 cents per hundredweight.

8 Since the time that our original proposal was
9 submitted, CDFA has released updated hauling rate
10 information and we have garnered various hauling rate
11 information from other industry sources, some of which has
12 been testified too already today.

13 Differing estimates of the cost of hauling milk
14 from the North Bay to the Bay Area pose a serious
15 challenge to setting appropriate allowance rates. Hauling
16 cost data reported by CDFA put the cost of hauling milk
17 from the North Bay to the Bay Area at 49.3 cents per
18 hundredweight. It is an interesting coincidence that this
19 rate is identical to the one that is reported for hauls
20 from the northern San Joaquin Valley to the Bay Area.
21 Alternatively, two different industry contacts have stated
22 the cost of hauling milk from the North Bay to the Bay
23 Area is approximately 60 cents per hundredweight.

24 How can we make sense of this apparent
25 discrepancy? Well, we have heard that the lower North Bay

1 to Bay Area rate is being supported by hauls from the San
2 Joaquin Valley. For example, a truck first takes a load
3 of milk to the Bay Area from the northern San Joaquin
4 area. After unloading the truck then proceeds to the
5 North Bay, assembles another load for delivery to the Bay
6 Area. This method of backhauling North Bay loads with
7 Central Valley loads apparently results in a lower total
8 overall cost and might be responsible for the rate
9 discrepancy that we have described. The fact that the
10 North Bay to Bay Area and the northern San Joaquin to Bay
11 Area rates are identical also fits well with this
12 explanation.

13 But whatever the reason for the hauling cost
14 discrepancy, it appears that both rates are valid and both
15 rates are representative of hauling costs that producers
16 in the North Bay can expect to be charged for shipments
17 into the Bay Area. The existence and validity of both
18 rates poses an interesting policy dilemma. If the lower
19 rate is used, then some plants in the Bay Area will be
20 disadvantaged in attracting milk supplies from the North
21 Bay and could well end up having to pay additional monies
22 to subsidize their producers' hauling costs.

23 On the other hand, if the higher rate is used,
24 then the plants whose producers are subject to the lower
25 rate will have an advantage over other Class 1 plants in

1 attracting milk. One response might be to simply say that
2 all plants should seek to contract with the lower cost
3 hauler in order to obtain the same rate. However, it is
4 not certain that new hauling contracts could be obtained
5 with hauling charges at the lower rates currently being
6 experienced by these plants.

7 The Department will have to reconcile this
8 situation because it alone has both the ability and
9 information to critically examine individual plant hauling
10 rates. In the following table, Table 1, we have attempted
11 to illustrate Dairy Institute's proposal under both of the
12 representative costs that been put forth for the North Bay
13 area to Bay Area haul. In setting our proposed allowance
14 rates under each scenario, we have employed data provided
15 to us by industry contacts about the local haul in the
16 North Bay as well as the cost of the haul from the North
17 Bay to the Solano receiving area.

18 In Table 1, proposed columns A and B illustrate
19 Dairy Institute's proposal under the assumption that the
20 allowance rates are to be set at the difference between
21 the local haul and the haul to the Bay Area -- fluid
22 plants. Proposal A assumes the cost of hauling to the Bay
23 Area from the North Bay is 60 cents per hundredweight,
24 whereas Proposal B assumes that the cost is 49.3 cents per
25 hundredweight.

1 Proposals C and D recognize the Department's
2 revealed preference for the formulation of allowance rates
3 that are omni-directional. That is, all producers who are
4 located at a fixed distance, for example, 75 miles, from a
5 deficit area plant receive the same transportation
6 allowance regardless of their relative direction from the
7 plant. In a proposals C and D, the allowance rates are
8 adjusted under the assumption that transportation
9 allowance for milk moving into Bay Area will remain at 24
10 cents for milk moving up to 99 miles, regardless of where
11 that milk is located.

12 Under proposal C, the assumed cost of hauling
13 from the North Bay to the Bay Area is 60 cents, for under
14 proposal D is 49.3 cents. In each of the proposals
15 presented, the net haul for the producer located in the
16 North Bay is the same whether he or she ships to the local
17 Class 1 plant, a plant in the Bay Area, or a plant in the
18 Solano receiving area.

19 We should note, however, that under proposal D
20 the transportation allowance rate for milk moving into
21 Solano would be significantly greater than it is
22 currently. Such a large increase in the allowance rate
23 could present additional competitive issues between the
24 Solano area plants and plants in Sacramento receiving
25 area. The Department needs to take these competitive

1 issues, as well as its unique knowledge of individual
2 plant hauling rates, into account when decided how to
3 implement the principle we have illustrated here.

4 And just kind of run through the table. What
5 I've got here is the information we have on the hauling
6 costs, from discussions we had with people in the
7 industry. From Sonoma to Marin to Sonoma to Marin rate of
8 39 cents. It's obviously a local haul.

9 When I say what is the implied allowance rate,
10 that basically is what is the difference between the hauls
11 to the fluid plant and the local haul.

12 And of course for Sonoma-Marin it's zero because,
13 you know, they're the same.

14 For Sonoma-Marin to the Bay Area the implied
15 allowance rate would be that -- the first column there
16 would be that 60-cent rate minus the 39. That should --
17 I'm sorry, that should say 21 cents, not 22 cents. So
18 that's how that's calculated.

19 And then the proposed amounts rates are what we
20 proposed under each of those scenarios.

21 The point here is we're trying to illustrate a
22 principle. And that's the principle that there's
23 competitive equity among these Class 1 plants that are
24 competing for the same milk supply.

25 And where those allowance rates actually end up

1 is going to be dependent upon what those actual costs are.
2 And what we have from the Department is sort of a weighted
3 average cost in particular areas for a particular point in
4 time. And there appear to be some discrepancies when you
5 look at individual plants. And I think what we're saying
6 is that the Department has the knowledge to figure out
7 where in that range the actual number ought to fall and
8 where the rates ought to fall and the importance of that.
9 We don't have those individuals numbers to testify to.

10 Moving on to other proposal. In general, Dairy
11 Institute supports proposals that seek to make
12 cost-justified adjustment to the transportation allowances
13 and credits. Dairy Institute believes that transportation
14 allowances and credits must be adequate to encourage milk
15 to move to higher-use plants in deficit areas. Inadequate
16 transportation allowance and credit rates can lead to
17 Class 1 markets being served by out-of-state suppliers to
18 the detriment of the California pool. Inadequate rates
19 also lead to California Class 1 processors being both
20 unable to compete favorably with manufacturing plants for
21 milk supplies and at a competitive disadvantage with
22 respect to out-of-state processors.

23 In order to secure the local Class 1 market for
24 California producers, transportation allowances and
25 credits must be adequate to draw milk without

1 transportation subsidization by the buyer or supplying
2 cooperative.

3 For this reason, and to foster competition among
4 Class 1 milk suppliers, Dairy Institute continues to
5 support the principle that transportation allowance rates
6 should be set equal to the difference between the cost of
7 the local haul and the cost of the haul to the more
8 distant higher-use plants. A slight shortfall should
9 apply only to the most distant mileage brackets to
10 encourage milk that is located closer to market to move
11 first.

12 In the case of transportation credits, they
13 should compensate the milk supplier for the cost of
14 shipping milk from the supplying plant to the deficit area
15 plant after accounting for any difference in marketing
16 area Class 1 differentials. Shortfalls in credit rates
17 again should be employed for the most distant milk and not
18 the milk in these relatively closer areas that regularly
19 serves the southern California Class 1 market.

20 Clover Stornetta farms: Clover's petition raises
21 some legitimate questions regarding the interplay between
22 transportation allowances and competitive equity among
23 Class 1 plants in the greater Bay Area market. However,
24 given either the new Department hauling cost data or the
25 hauling cost data from industry sources, the proposed

1 allowance rate of 24 cents per hundredweight, which was in
2 their original petition, would appear to overcompensate
3 producers shipping to Class 1 plants in Sonoma and Marin
4 counties. Determining the appropriate allowance rate will
5 be dependent on discovering the true cost of shipping milk
6 to the Bay Area from the North Bay as we have discussed
7 earlier.

8 Once the appropriate rate is determined, it could
9 be implemented by creating a new North Bay receiving area,
10 as we have suggested, or by including Sonoma and Marin
11 counties in the Bay Area receiving area and defining a new
12 mileage bracket, such as zero to 40 miles, with a lower
13 transportation allowance rate that would adequately
14 address any competitive inequities fostered by the current
15 allowance rate system.

16 California Dairies: Dairy Institute supports
17 cost-justified allowances and credits. CDI's proposal for
18 an allowance of 34.75 cents per hundredweight appears to
19 be based on a North Bay to Bay Area haul of 60 cents and
20 an assumed local haul rate of 25.25 cents. As the local
21 haul rate in the North Bay is higher than what was assumed
22 by CDI, we do not support their proposed allowance rate
23 for milk moving from the North Bay into the Bay Area.

24 With regard to CDI's proposed changes to
25 allowance rates in southern California, we are generally

1 supportive of their proposed rates in the zero to 89 miles
2 bracket and the 89 to 139 miles bracket. But CDI's
3 proposed allowance rates on the highest mileage bracket
4 appears to employ a shortfall of about 10 cents per
5 hundredweight based on the CDFA data that we were looking
6 at. We would argue that since milk moves regularly from
7 more than 139 miles to serve the Class 1 market,
8 shortfalls should be no more than a few cents. Dairy
9 Institute is supportive of CDI's proposed adjustments to
10 transportation credits for milk and condensed skim sourced
11 at plants in Los Angeles County.

12 Land O' Lakes: Dairy Institute generally
13 supports LOL's proposed adjustments to credits and
14 allowances for bulk milk to the extent they are cost
15 justified. However, increases in transportation credits
16 applicable to milk and condensed skim shipments from
17 supply plants in Tulare County must be accompanied by
18 adjustments in the transportation credits applicable to
19 milk and condensed shipments originating in plants in Los
20 Angeles so that competitive parity is maintained.

21 With respect to transportation allowances on milk
22 moving from the South Valley into southern California, we
23 believe the shortfall of approximately 13 cents in the
24 over 139 miles bracket is excessive. Again, the allowance
25 rate should more closely align with the cost difference

1 between the local haul and the haul to the higher-use
2 plants in southern California, with any shortfall being no
3 more than a few cents.

4 Dairy Farmers of America: Dairy Institute
5 generally supports DFA's proposal to increase
6 transportation allowances for milk moving into the Solano
7 receiving area to the extent that such changes are cost
8 justified being here. However, the proposed rates could
9 create some competitive inequities with other Class 1
10 plants, particularly with respect to milk in North Bay and
11 southern Sacramento and San Joaquin counties.

12 The inequities could be addressed through
13 adjustments to the mileage brackets applicable to the
14 Solano receiving area. For example, Petaluma is located
15 approximately 40 miles from the Solano plant. But
16 Sebastopol, which is also part of the North Bay milk
17 supply area, is located 59 miles from the Solano plant. A
18 mileage bracket that breaks at 44 miles would split the
19 Sonoma milk supply and perhaps encourage more distant milk
20 to be shipped rather than closest milk to the Solano plant
21 since a higher allowance would apply to that more distant
22 milk. A mileage bracket structure that applies the lowest
23 rate for zero to 60 miles, the next lowest rate for over
24 60 to 99 miles, and then a highest rate for hauls over 99
25 miles should address some of the competitive problems

1 posed by DFA's proposed allowance rates.

2 Security milk producers: Dairy Institute
3 supports the allowance rate changes proposed by Security
4 to the extent that they are cost justified and conform to
5 the general principles we've outlined earlier in our
6 testimony. We do note that the proposed allowance rate
7 for the "over 139 miles" mileage bracket appears to
8 overcompensate producers for the difference between the
9 local haul cost and the southern California haul cost by 2
10 to 3 cents per hundredweight per CDFA data.

11 Call provisions: Dairy Institute supports the
12 continuation of the call provisions. Under these
13 provisions, handlers are given an incentive to voluntarily
14 supply milk for fluid uses when call provisions are
15 implemented. The existence of the call provisions
16 promotes supply handlers building business relationships
17 with fluid customers to voluntarily release market milk
18 such that both seller and buyer can better plan such milk
19 shipments. Without the call provisions, supply handlers
20 have less incentive to build such ongoing relationships,
21 which could exacerbate disorderly and chaotic milk
22 movements in emergency short supply situations.

23 Dairy markets are unpredictable and the call
24 provisions are necessary as a standby mechanism should
25 they be rapidly and expectedly needed. Unanticipated

1 weather conditions, rapidly changing manufactured product
2 prices, and cost/price squeezes have caused sudden changes
3 in milk production patterns in the past and the call
4 provisions have helped maintain milk supply availability.
5 The call provisions are the only means within the
6 marketing and pooling system to make quota milk available
7 for priority uses.

8 Regional quota adjusters: Dairy Institute
9 supports a continuation of the RQAs on the grounds that
10 our membership believes that quota holders have an
11 obligation to ensure that Class 1 markets are served.
12 RQAs provide, albeit indirectly, pool revenues that are
13 available to fund transportation allowances and credits.
14 We do not support any changes to the RQAs at this time.

15 Thank you for the opportunity to testify. I
16 would like to request the opportunity to file a
17 post-hearing brief. And I'm willing to answer any
18 questions you may have at this time.

19 HEARING OFFICER ESTES: Your request is granted.
20 Please provide it to the Department, as previously
21 mentioned here in today's hearing.

22 Do we have questions from the panel at this time?

23 DAIRY MARKETING BRANCH ACTING CHIEF ERBA: Dr.
24 Schiek.

25 DR. SCHIEK: Yes, Dr. Erba.

1 DAIRY MARKETING BRANCH ACTING CHIEF ERBA: Rather
2 than go forward with what you proposed, to create a new
3 North Bay receiving area, are you consenting to changing
4 the Bay Area receiving area by simply by adding a third
5 mileage bracket an including Sonoma and Marin counties as
6 part of the receiving area?

7 DR. SCHIEK: No, I think we would still prefer to
8 see a separate North Bay receiving area. But what we're
9 saying is, if the Department prefers simplicity, I
10 suppose, fewer numbers of receiving areas, the competitive
11 issues could be accommodated in a manner similar to what
12 was proposed by Clover today, which was, you know, using a
13 different mileage bracket and including them with the Bay
14 Area, and a lower allowance rate.

15 So it's an alternative, what we're saying, to
16 address the situation. But we still think a separate
17 receiving area makes more sense.

18 DAIRY MARKETING BRANCH ACTING CHIEF ERBA: Okay.
19 When you spoke to DFA's proposal you had suggested
20 changing some mileage brackets --

21 DR. SCHIEK: Yeah.

22 DAIRY MARKETING BRANCH ACTING CHIEF ERBA:
23 -- where they currently exist?

24 I understand what you're trying to do there.

25 Did you want to -- are you in support of DFA's

1 newly proposed rates or the current rates?

2 DR. SCHIEK: Like I say, we're supportive of
3 making adjustments to those rates 1) if they're cost
4 justified and 2) subject to the competitive concerns in
5 the North Bay area that we've outlined. So, basically
6 we're looking at their rates and the numbers they've
7 provided, which I can't necessarily comment on, you know,
8 their accuracy. And, unfortunately, although Mr. Tillison
9 did an admirable job reading their testimony, he's not
10 able to answer questions specific to those rates. But,
11 you know, the rate -- the proposed rates appear to be cost
12 justified. So the only modification would be, you know,
13 depending on how -- what you determine the appropriate
14 haul rate from North Bay into the Bay Area is, you would
15 adjust the allowance rates in Solano, in the North Bay and
16 in the Bay Area so that there's a net haul rate for
17 producer in the North Bay shipping in those plants that's
18 virtually identical.

19 DAIRY MARKETING BRANCH ACTING CHIEF ERBA: DFA
20 also testified that they would support and promote no
21 shortfall in any of the mileage brackets. You seem to
22 indicate that there should be at least some shortfall.
23 Can you speak to that?

24 DR. SCHIEK: The -- I think we would be frankly
25 not opposed to a no-shortfall concept. But I recognize

1 that there's a desire to ensure milk closer in moving
2 first.

3 DAIRY MARKETING BRANCH ACTING CHIEF ERBA: Sure.

4 I think we tend to take a little bit broader
5 view, because one of the issues is some times it closes --
6 in-milk is controlled by one supplier. And when there's a
7 strong disincentive on the farther away milk versus that,
8 it creates a market power situation for the supplier that
9 controls the closer-in milk. And our view is that -- you
10 know, that may be okay for a while. But at some point
11 depending on the behavior of that supplier, processors may
12 be encouraged to look for milk supplies out of state if
13 they can get them cheaper. And our view is the more
14 competition there is among the California suppliers for
15 that Class 1 milk, the more likely it is that we're going
16 to be able to supply Class 1 plants in California with
17 California milk.

18 DAIRY MARKETING BRANCH ACTING CHIEF ERBA: Right.

19 Thank you.

20 MILK POOLING BRANCH CHIEF LEE: Regarding CDI's
21 testimony regarding condensed -- transportation credits on
22 condensed skim -- movement of condensed skim, what's the
23 Dairy Institute's feelings on that issue?

24 DR. SCHIEK: I knew you were going to ask me
25 this.

1 If your memory is better than mine, you probably
2 will remember that at the hearing on transportation
3 allowance and credits a year ago we opposed including
4 credit for condensed skim. Our argument was that
5 historically we haven't had credit for condensed skim, and
6 so relationships had been developed for procurement of
7 condensed skim that didn't necessarily match up with local
8 milk sheds; and, therefore, there was an incongruity
9 between local milk sheds and allowances in credits and
10 where condensed skim is normally procured. So that was
11 why was we opposed it.

12 However, now that we've had it for a year, and
13 people's contracts and procurement patterns have changed,
14 I think probably what we would argue for is regulatory
15 consistency. I mean now that people have contracts in
16 place, they are responding to these condensed skim
17 credits. To then yank them out I think is disruptive.
18 And so I think at this point we would argue for their
19 continuance.

20 MILK POOLING BRANCH CHIEF LEE: Thank you.

21 MILK POOLING RESEARCH MANAGER SHIPPELHOUTE: No
22 questions.

23 HEARING OFFICER ESTES: Any additional questions?

24 All right. Thank you for your testimony.

25 HEARING OFFICER ESTES: Before we proceed to Land

1 O' Lakes we're going to take a five-minute break.

2 I also might note for those -- the rest of you
3 that are here, if you have not signed the witness list and
4 if you want to testify today, please go to the back of the
5 room to do so.

6 (Thereupon a recess was taken.)

7 HEARING OFFICER ESTES: All right. We are
8 reconvening at this time. So if people would please sit
9 down and allow us to commence the hearing.

10 All right. We're going to procedure with the
11 alternative petition for Land O' Lakes at this time.

12 Do you swear or affirm to tell the truth and
13 nothing but the truth today?

14 MR. GRUEBELE: I do.

15 HEARING OFFICER ESTES: Could you please state
16 your name and spell your last name for the record.

17 MR. GRUEBELE: James Gruebele G-r-u-e-b-e-l-e.

18 HEARING OFFICER ESTES: And could you -- you're
19 here appearing on behalf of Land O' Lakes today. Could
20 you describe the basis by which you've been authorized to
21 represent them today.

22 MR. GRUEBELE: My testimony was approved by the
23 Board of Directors.

24 HEARING OFFICER ESTES: I see you've introduced a
25 written statement, which I assume will conform to your

1 comments here today?

2 MR. GRUEBELE: I will probably skip some of the
3 comments verbally. But I expect that the written comments
4 will all be included.

5 HEARING OFFICER ESTES: All right. So we will
6 introduce them into the record as Exhibit No. 50.

7 (Thereupon the above-referred to document
8 was marked by the hearing officer as
9 Exhibit 50.)

10 HEARING OFFICER ESTES: And you have half an hour
11 to present your testimony today in support of the Land O'
12 Lakes alternative petition.

13 MR. GRUEBELE: Pardon?

14 HEARING OFFICER ESTES: You have half an hour to
15 present testimony in support of the alternative position
16 by Land O' Lakes.

17 And please proceed.

18 MR. GRUEBELE: My names is James W. Gruebele,
19 Dairy Industry Consultant, 7196 Secret Garden Loop,
20 Roseville, California. I am testifying on behalf of Land
21 O' Lakes, which handles about 14 million pounds of milk
22 per day and has a California membership of about 249
23 producers. This excludes Orland. There are ten producers
24 that operate dairies in southern California as members of
25 our cooperative. We appreciate the call of the hearing on

1 a very important issue.

2 And I won't read the rest of that. I think we
3 know what the purpose of the hearing is. So I'll just go
4 on to Land O' Lakes' proposal.

5 Our alternative proposal is to amend the southern
6 California milk stabilization plan by adjusting the
7 transportation credit for Riverside and San Diego Counties
8 and for Los Angeles, Orange and Ventura counties.

9 The specific proposal is as follows:

10 We propose to increase the transportation credit
11 from 60 pent 75.25 cents per hundredweight for milk moving
12 on a plant-to-plant basis from Tulare County to Los
13 Angeles, Orange and Riverside counties.

14 Sorry. I'll correct that statement.

15 Please note that it should say Ventura stead of
16 Riverside.

17 Secondly, we propose an increase in the
18 transportation --

19 HEARING OFFICER ESTES: Excuse me, Dr. Gruebele.
20 Could you do me a favor. Could you refer to the line in
21 your testify where that's located.

22 MR. GRUEBELE: Yes, it looks like it's 1, 2, 3,
23 4, 5 -- the 6th line, it says, "Riverside counties." It
24 should say, "Ventura."

25 HEARING OFFICER ESTES: Okay.

1 MR. GRUEBELE: Secondly, we propose an increase
2 in transportation credit from 68 to 83.5 cents per
3 hundredweight for milk moving from Tulare County to
4 Riverside and San Diego counties. We also are proposing a
5 transportation credit for condensed skim at 81.25 cents
6 per hundredweight for condensed skim moving from Tulare to
7 Los Angeles, Orange and Ventura counties and a 89.5 cent
8 per hundredweight credit for condensed skim from Tulare
9 County to Riverside and San Diego counties.

10 The math is as follows: The current hauling rate
11 on a plant-to-plant basis from Tulare to Los Angeles,
12 Orange and Ventura counties is \$1.0225 per hundredweight
13 and the current area differential is 27 cents per
14 hundredweight, a difference of 66 cents per hundredweight.
15 The current transportation credit is 60 cents per
16 hundredweight, so we -- so there's a shortfall of 15.25
17 per hundredweight.

18 I believe the -- I see another typo. And that's
19 in the second full paragraph, 1, 2, 3 -- the 4th line. A
20 difference of 66 cents per hundredweight should say 75.25
21 cents per hundredweight. I apologize.

22 The hauling rate for milk on a plant-to-plant
23 basis from Tulare to Riverside County is \$1.105, and the
24 current area differential again is 27 cents on the
25 hundredweight, a difference of 83.5 cents per

1 hundredweight. And -- and that is correct.

2 The current transportation credit is about 68
3 cents per hundredweight. Leaves us a shortfall of 15.5
4 cents per hundredweight for milk hauled from Tulare to
5 Riverside County.

6 On condensed, the hauling rate are the same as
7 stated above. However, the area differential for Class 1
8 is on the fluid side. The difference in the fluid price
9 between southern California and northern California is
10 .0031 per pound. Condensed skim is 32 percent solids,
11 leaving 68 pounds of fluid carrier. The area differential
12 for condensed skim is 21 cents per hundredweight, which is
13 achieved by multiplying 68 pounds times .0031 per pound of
14 fluid carrier.

15 Therefore we are proposing a transportation
16 credit of 81.25 cents per condensed skim shipped from
17 Tulare to Los Angeles, Orange and Ventura counties and
18 transportation credit of 89.5 cents for condensed skim
19 shipped from Tulare to Riverside and San Diego counties.

20 The language reads as in down -- as stated in the
21 Milk Stabilization Plan, so I will not reread all that
22 information.

23 To sum up the information by the maximum
24 production per pound: Tulare County, 89.5 cents to
25 Riverside or San Diego counties; and Tulare County to

1 Orange, Los Angeles and Ventura counties. We are not
2 necessarily objecting to and adjustment for Los Angeles
3 County. We had no basis to make any recommendation
4 because we didn't have any hauling costs information for
5 Los Angeles County and San Diego, Riverside, Orange or
6 Ventura counties. So that's why we left it at 24 cents
7 per hundredweight.

8 The schedule for condensed skim is Tulare County
9 to Riverside or San Diego counties, is 89.5; and from
10 Tulare County to Orange, Los Angeles or Ventura counties
11 is 81.25.

12 Transportation allowance proposal:

13 To make California more competitive with
14 out-of-state sources and to provide more producer equity,
15 we are recommending two important changes in
16 transportation allowance. One is to change the current
17 transportation allowance to account for the increased
18 hauling costs.

19 And the second is to limit the supply counties
20 for the transportation allowance system. Based upon the
21 local haul to manufacturing facilities and the long
22 distance haul to Class 1 plants in southern California, we
23 are proposing an adjustment in the transportation
24 allowance from 43 cents to 47.75 cents per hundredweight
25 for the mileage bracket between 89 to 139 miles from the

1 South Valley to southern California markets.

2 Land O' Lakes is not moving milk on a
3 ranch-to-plant basis from Tulare County. But CDI has
4 requested an adjustment in the transportation allowance to
5 cover producers over the 139 miles. We have no objection
6 to their request. For plants located in the southern
7 California receiving area which shall consist of counties
8 Los Angeles, Mono, Orange, Riverside, San Bernardino and
9 Ventura counties that from zero to 89 miles the
10 transportation allowance should remain at 9 cents per
11 hundredweight and over 89 miles the transportation
12 allowance should be established at 20 cents per
13 hundredweight.

14 The reason for the 20 cents is it represents the
15 difference between the local haul to the manufacturing
16 facility and the longer distance haul to a Class 1 plant
17 in the deficit area.

18 The current transportation allowance of 43 cents
19 per hundredweight from 89 to 139 miles is simply too large
20 for producers located in high desert region. Those
21 producers are overcompensated for the haul cost to the
22 Class 1 plant in southern California.

23 While we realize the Department has changed
24 policy somewhat to use concentric circles in establishing
25 transportation allowances, we would argue the principle of

1 the short distance haul to a manufacturing plant and a
2 longer distance haul to a Class 1 plant is still being
3 utilized by the Department to establish transportation
4 allowances for Kern and Tulare counties.

5 For the sake of consistency it would seem
6 reasonable to apply that principle to say milk being
7 shipped from the San Bernardino County to deficit Class 1
8 distributing plants in southern California.

9 We recommend the elimination of Fresno County and
10 all other counties not listed below as supply counties for
11 the transportation allowance system. Based upon the
12 information available, there are more than adequate
13 amounts of milk available from Kern and Tulare counties to
14 supplement the Class 1 requirements of fluid milk
15 operations in southern California on a ranch-to-plant
16 basis.

17 Section 921:

18 I won't read that language. I'll simply go to
19 Item No. 1 on page 4.

20 From Inyo, Los Angeles, Mono, Orange, Riverside,
21 San Bernardino and Ventura counties, the following
22 transportation allowances will apply: From zero to 89
23 miles, 9 cents per hundredweight; over 89 miles, 20 cents
24 per hundredweight.

25 From Santa Barbara, San Diego, Imperial, Kern,

1 Kings and Tulare counties, from zero to 89 miles, 9 cents
2 per hundredweight; from 89 to 139, 47.75 cents; and over
3 139, 58 cents per hundredweight. But I already stated in
4 my formal testimony that we don't object -- we didn't have
5 the numbers because we didn't haul milk in Tulare -- we
6 don't object to the CDI proposal.

7 For San Diego, the same rate, 9 and 20, apply.

8 And the same rates apply from zero to 89, 89 to 139, over
9 139, again with the caveat that was stated before.

10 Justification:

11 Southern California is a deficit market. There
12 has usually been a shortfall on the transportation credit
13 program in California. In light of the increased need for
14 out-of-area milk in southern California due to the dairies
15 moving from southern California into other California
16 areas and to out-of-state locations and the dramatic
17 increased threat of out-of-state milk as a source of milk
18 for California processors, we are advocating no shortfall
19 in the transportation credit program.

20 Milk needs to move from surplus producing areas
21 in the South Valley to southern California either on a
22 plant-to-plant or ranch-to-plant basis. Tables 1 of the
23 7m tables made available by the Department at the last
24 hearing make the point. I realize that time is limited,
25 but for an historical standpoint, the document prepared

1 for the 2003 hearing has valuable information, and we
2 would be grateful if the Department updated that
3 information because it is useful to identify sources of
4 milk. And we as an industry would really appreciate it.

5 This is especially important now because of the
6 recent court decision. Is other source milk growing as a
7 result of the Court decision? Based upon information made
8 available in the pre-hearing workshop for April 2004, the
9 direct shipment of milk on a daily basis from southern
10 California ranches to southern California plants totaled
11 11,380,831 pounds per day. But the direct shipments from
12 northern California to southern California plants amounted
13 to 6,596,507 pounds on a daily basis.

14 The plant transfer from northern California to
15 southern California amounted to 1,599,401 pounds per day.
16 The bad news is that the other source of milk -- this is
17 using March 2004, the last time it was reported --
18 amounted to 3,504,288 pounds per day. The amount of other
19 source milk, out of state, was twice as large as the plant
20 transfers from northern California to southern California.

21 Assuming that all the other source milk in March
22 2004 had been utilized in southern California -- and we
23 know that is not the case -- then the other source milk
24 plus northern California milk, both ranch-to-plant and
25 plant-to-plant, would represent about 50 percent of the

1 total milk used in southern California. In other words,
2 southern California is definitely a deficit market and is
3 becoming more so.

4 Producer milk used for Class 1 purposes is paid
5 the highest price. But this means that the producers have
6 the responsibility to serve that market and to support the
7 milk movement programs to ensure there are adequate
8 amounts of milk available for Class 1 processors at class
9 prices plus a reasonable service charge.

10 Equal raw product costs:

11 To maintain equal raw product costs for
12 California fluid operations it is necessary to update the
13 transportation credit to reflect the cost of moving milk
14 from Tulare into southern California. And I won't repeat
15 those numbers because really I verbalized them before, so
16 I don't need to repeat that.

17 As everyone knows, packaged milk is being
18 imported -- this is the last phrase on page 5 -- milk
19 imported into a California plant from a plant in Arizona
20 that is totally unregulated. This is going to be a very
21 serious problem for plants that are required to pay the
22 southern California Class 1 milk price used for fluid
23 purposes. In addition, we all know about the court case
24 with respect to other source milk. This milk is no longer
25 pooled. It is extremely important that we make

1 adjustments to the transportation allowance and credits in
2 order to compete more effectively with out-of-state bulk
3 and packaged milk.

4 Historical Precedence:

5 The Department of Food and Agriculture from a
6 historical standpoint has always made cost-justified
7 adjustments in transportation credit or area differential
8 to enable the movement of milk on a plant-to-plant basis.

9 The Departmental Exhibit 7d Table 1 shows a
10 summary of changes in transportation credits and area
11 differentials. Starting in 1980 the area differential was
12 55 cents per hundredweight, which at that time reflected
13 the cost of plant transfers.

14 In 1981, the concept of transportation credit was
15 introduced. Instead of increasing the area differential
16 from 55 to 61 cents, the decision was made to establish a
17 transportation credit of 6 cents per hundredweight.

18 The chart shows that the area differential was
19 decreased from 55 to 40 cents in August 1982, but the
20 transportation credit increased from 6 cents to 22 cents
21 per hundredweight.

22 In 1983, the combination of the area differential
23 and the transportation credit decreased by 2 cents per
24 hundredweight. In 1984, however, it was increased by 2
25 cents. In 1988, there was another 2 cent increase, and in

1 1989 there was another 2 cent increase, and another 1 cent
2 increase in 1991. There was a 5 cent increase in 1994.

3 In 1996, the area differential was reduced to 27
4 cents, but the transportation credit moved from 27 cents
5 to 50 cents per hundredweight. So the total compensation
6 was increased by a total of 4 cents per hundredweight.

7 The transportation credit in 2003 was increased
8 from 50 to 60 cents per hundredweight for milk moved from
9 South Valley into the Los Angeles deficit market. And
10 there was a separate transportation credit of 68 cents for
11 milk moved into Riverside County.

12 This history clearly shows the Department was
13 willing to make cost-justified adjustments in the area
14 differential and/or transportation credit.

15 Plant-to-plant milk movement is efficient:

16 Historically, Land O' Lakes has supplied our
17 customers with standardized milk products. In the case of
18 Los Angeles County plants, this tends to be skim milk. In
19 the case of the Riverside plant, it is 2 percent milk, 1
20 percent milk, or whatever their needs are. In any case,
21 because of the California standards it is necessary to add
22 solids to the milk and, furthermore, the lower fat
23 products are very prominent. The supplying of
24 standardized products avoids the unnecessary movement of
25 unneeded fat in both directions. In any case, a large

1 manufacturing plant like Land O' Lakes are highly
2 efficient in performing the functions like separating milk
3 into cream and skim, and they are highly efficient in
4 producing condensed skim.

5 Our contention has always been that the
6 plant-to-plant milk movement was a very efficient way to
7 service the southern California market. And the study
8 that -- I didn't refer to in this particular testimony but
9 in a previous testimony, the study by the Department
10 reinforces our contention.

11 Tailored milk for Riverside County:

12 Our Riverside customer buys tailored milk from
13 Land O' Lakes' operation in Tulare. Our other customers
14 buy standardized product like skim milk. The reason is
15 obvious. There's a greater need for skim and solids than
16 there is for fat. While some may argue you this provides
17 an advantage to these plants, our observation is that this
18 opportunity for tailored milk is available to all
19 processing plants.

20 Secondly, our customers pay for standardization.
21 Our customers do receive milk from ranch to plant. But
22 the standardized products can be made available only on a
23 plant-to-plant basis. In the case of one of our Los
24 Angeles customers, a considerable amount of product on
25 plant-to-plant movement is skim milk. The tailoring of

1 milk is an efficient way to service a fluid operation in
2 the southern California market.

3 I'm going to skip the rest of page 7, all of page
4 8, and go to page 9.

5 Land O' Lakes is not competitive in California:

6 If Land O' Lakes charges customers enough to
7 cover the shortfall in the transportation credit, then our
8 customers will have higher raw product costs than their
9 competitors.

10 Land O' Lakes needs to be competitive with
11 out-of-state sources:

12 It is extremely important that California milk is
13 competitive with out-of-state sources. And that certainly
14 includes the plant-to-plant shipments from Land O' Lakes
15 to Class 1 milk plants in Los Angeles and Riverside
16 counties. This is now even more important because of the
17 recent court decision. As mentioned earlier, Schedule 1
18 shows Table 1 of 7m tables made available by the
19 Department for the 2003 hearing.

20 This schedule shows the direct shipments from
21 southern California to southern California plants on a
22 daily basis from July 1985 through March 2003. It shows
23 the direct shipments from northern California to southern
24 California plants for the same period. It shows the plant
25 transfers from northern to southern California plants for

1 the same period. It shows the shipments and transfers
2 from other sources on a daily basis from January 1993
3 through March 2003.

4 It also shows the production of exempt milk and
5 plant transfers from southern California to northern
6 California. The data clearly show that plant transfers
7 have been reasonably consistent for this entire period.
8 The volume transferred in this way exceeded two million
9 pounds per day in early 1987 and again in 1989 and in
10 1990; then it declines somewhat by 1998, then reached a
11 low point in early 2001. But since September 2001 the
12 volumes again grew to over two million pounds per day.
13 The volume for March 2003 was one and a half million
14 pounds per day. The bad news is that there was almost
15 twice as much milk being shipped into California from
16 out-of-state sources than is being supplied on a plant
17 transfer basis in California.

18 The other source milk has been growing. We did
19 an analysis of the overall pool effect of out-of-state
20 sources of milk. The impact in May 2002 was approximately
21 6.7 cents per hundredweight and the impact for January
22 2003 was 6.5 cents per hundredweight. The total cost to
23 California for out-of-state milk totals \$19 million for
24 all of 2002. It was almost \$2 million for January 2003.

25 The Department estimated the cost of Land O'

1 Lakes' proposal for a transportation credit adjustment.
2 Their estimate shows that the monthly additional cost to
3 the pool would be about \$70,000. For May 2004 this added
4 cost would amount to about .0023 per hundredweight as far
5 as the overall pool is concerned.

6 What if the amount of milk transferred by Land O'
7 Lakes was going to be supplied by out-of-state sources?
8 Depending on the month used, the analysis shows it would
9 be far more costly to lose those Class 1 sales to
10 out-of-state sources. My estimate is that it would cost
11 at least ten times more.

12 The decision on the transportation credit as a
13 result of this hearing, in my opinion, will have important
14 implications on the competitive position of California
15 sources of milk as compared to out-of-state sources for
16 milk for Class 1 milk purposes.

17 Justification for the changes in the
18 transportation allowance:

19 Again, as in the transportation credit program,
20 it is essential to adjust the transportation allowance in
21 California when the hauling rates warrant such changes.
22 Plants in the deficit markets need the producer milk and,
23 in fact, the needs are greater today than in the past
24 because of the continued exodus of producers from the
25 southern California milk shed.

1 Again, California needs to be competitive with
2 out-of-state sources of milk and so needed adjustment
3 should be made so that producers in the relevant supply
4 areas are no longer -- are no worse off supplying Class 1
5 plants than supplying milk to a manufacturing facility.
6 It is important to encourage milk to move for Class 1
7 purposes. However, as mentioned earlier, there are cases
8 where the Departmental policies have resulted in some
9 producers being overcompensated in moving milk to Class 1
10 milk plants. For the sake of producer equity, for over 89
11 miles the transportation allowance should be adjusted to
12 20 cents instead of the current 43 cents for producers in
13 the Barstow area shipping milk into Class 1 milk plants.

14 I want to reemphasize that point in the next
15 paragraph.

16 Reliable sources indicate the hauling rate from
17 Barstow area to the greater Los Angeles area is 54 cents.
18 For over 89 miles to 139 miles the current transportation
19 allowance is 43 cents. And if the Department grants an
20 increase by a number of the hearing participants today to
21 about 48 cents for over 89 miles and less 139 miles, then
22 the net haul cost for these producers will be only 6 cents
23 per one hundredweight. Where in all of California is
24 there a hauling cost of only 6 cents per hundredweight for
25 moving milk? From a producer equity standpoint, Land O'

1 Lakes believes that the transportation allowance from the
2 Barstow area should be reduced from the current 43 cents
3 to 20 cents per hundredweight.

4 It is extremely important to have programs built
5 on principles under a state or federally regulated system.
6 This in large part has been adhered to by the Department
7 of Food and Agriculture. Over the years, for example, the
8 Department used the area differential to reflect changes
9 in freight costs for plant transfers of milk from the
10 surplus producing area into deficit markets. From the
11 standpoint of location economics, this program policy made
12 sense. The location differentials were used to compensate
13 for the ranch-to-plant movement of milk.

14 The principle there was that the producer should
15 be not disadvantaged for serving the Class 1 milk market.
16 Therefore under the current transportation allowance
17 program the producer should be compensated for the
18 difference between the long distance haul to a Class 1
19 plant and the shorter distance to a manufacturing
20 facility.

21 The California producers have a responsibility to
22 ensure that all Class 1 needs of the California process --
23 or the milk processors are met. And in California this
24 includes the provision to pay for the milk incentive
25 programs. Pooled manufacturing plants also have a

1 responsibility to make milk available for Class 1 purposes
2 where there is a need to do so.

3 Plants must be willing to give up milk for Class
4 1 purposes where there's a need. All pooled manufacturing
5 plants in California have that responsibility. However,
6 just as in the case of the ranch-to-plant movement of
7 milk, the plants should not be disadvantaged in moving
8 that milk into Class 1 plants on a plant-to-plant basis.

9 The economic theory referred to earlier called
10 for a price difference between the surplus and deficit
11 markets that is large to cover the cost of freight in
12 moving milk into Class 1 distributing plants. The plants
13 using the transportation credit program should be
14 compensated for the freight costs in moving milk to
15 market. In any case, a manufacturing cooperative like
16 Land O' Lakes should be able to charge reasonable service
17 charge to compensate for the services rendered, like
18 standardizing milk, and for making milk available when
19 needed.

20 Even when those reasonable service charges are
21 made, it does not compensate a firm like Land O' Lakes for
22 the opportunity costs for processing manufactured products
23 when giving up that milk for Class 1 purposes. In my
24 opinion, that should be enough of a cost to pay for the
25 privilege of being pooled under the California system.

1 But more than anything else, California producers
2 face significant competition from out-of-state sources.
3 This is a major challenge. Adjustments to the
4 transportation credit and allowance program may be only a
5 small part of the solution to the out-of-state milk
6 problem.

7 The cost for not adhering to these principles
8 could be very large. We must remember that out-of-state
9 producers have an incentive under statute to move milk
10 into California because of the difference between the
11 California Class 1 price and the blend prices in whatever
12 market such producers might be located. The amount of
13 out-of-state milk has been growing.

14 And depending on the final outcome of court
15 proceedings, appeals and the like makes the out-of-state
16 milk problem a major problem. We need to do everything we
17 can to make California milk more competitive with
18 out-of-state sources. Making the needed adjustments to
19 the transportation credit and allowance programs can help
20 to do this.

21 The final principle is that the Class 1 handlers
22 must be able to achieve equal raw product costs. This is
23 always a challenge in a market that is deficit. The
24 adjustment of the transportation credits in southern
25 California will help to accomplish this goal.

1 We appreciate your call of the hearing.

2 HEARING OFFICER ESTES: Do you want the
3 opportunity to file a post-hearing brief?

4 MR. GRUEBELE: Yes, we would.

5 HEARING OFFICER ESTES: Okay. Your request is
6 granted.

7 Do we have any questions at this time?

8 MILK POOLING BRANCH CHIEF LEE: Just for
9 clarification.

10 Mr. Gruebele, on page 2 of your testimony you
11 mentioned a maximum deduction program from Los Angeles
12 County to the designated counties of 24 cents.

13 Is the current rate -- should it be 34 cents?
14 Just for clarification.

15 MR. GRUEBELE: Thank you. Yes. Sorry about
16 that.

17 MILK POOLING BRANCH CHIEF LEE: But you weren't
18 asking for 34 --

19 MR. GRUEBELE: Yes. And we had no basis for
20 changing it to 34 cents, that's correct.

21 MILK POOLING BRANCH CHIEF LEE: Thank you.

22 DAIRY MARKETING BRANCH ACTING CHIEF ERBA: Dr.
23 Gruebele, in a number of your calculations for how you
24 came up with the proposal, you used a haul rate from
25 Tulare to Los Angeles or into Ventura counties of \$1.0225.

1 And yet I see no justification as to where that number
2 came from. Can you explain where you got that number?

3 MR. GRUEBELE: That number came from Kings County
4 Truck Lines. I called them and got the rate.

5 And in my post-hearing brief I will supply the
6 documentation to support that.

7 DAIRY MARKETING BRANCH ACTING CHIEF ERBA:

8 Excellent. And I would have asked you to supply
9 the documentation.

10 MR. GRUEBELE: Thank you.

11 DAIRY MARKETING BRANCH ACTING CHIEF ERBA: You
12 trumped me again.

13 On page -- starting on page 3 -- you've actually
14 mentioned it several times throughout your written
15 testimony and your spoken testimony -- the idea that the
16 producers in the high desert area are overcompensated.

17 Do you know how much milk is coming in from the
18 high desert?

19 MR. GRUEBELE: I think that there was some
20 documents that were provided in the pre-hearing workshop.
21 But I don't remember what the number is, no.

22 DAIRY MARKETING BRANCH ACTING CHIEF ERBA: Okay.
23 My concern is that -- and the overcompensation for those
24 particular -- that particular group of producers had been
25 mentioned in this hearing and in previous hearings as

1 well. My concern is that we're going to cast a net, a
2 very large net to catch a very small number of fish. What
3 I mean by that is you're going to change a bracket that
4 applies to a large number of producers and a large volume
5 of milk to correct a problem which I think is a pretty
6 small number of producers and a pretty small volume of
7 milk.

8 Is there a better way of doing that than trying
9 to adjust this large bracket to address what I think is a
10 fairly small problem?

11 MR. GRUEBELE: Well, I'm not sure I understand
12 your point, other than to say that I have specifically
13 identified that the rate from Los Angeles, Mono, Orange,
14 Riverside, San Bernardino, and Ventura counties identified
15 the source -- if that helps any -- and adjust the over 89
16 miles to be 20 cents per hundredweight.

17 Does that satisfy your question?

18 DAIRY MARKETING BRANCH ACTING CHIEF ERBA:

19 Perhaps it will. I'm not very sure about that.

20 MR. GRUEBELE: What I'm saying is the over 89
21 miles for -- from Santa Barbara, San Diego, Imperial,
22 Kern, Kings, and Tulare counties would still be -- we are
23 proposing should be increased from 43 to 47.75. What I'm
24 suggesting is we identify the county of source as well as
25 the destination to adjust for the 89 miles for the Barstow

1 area.

2

3 DAIRY MARKETING BRANCH ACTING CHIEF ERBA: Okay.

4 And then maybe that would take care of the problem. I'm
5 not sure. Thank you.

6 I have no further questions. Thank you.

7 MILK POOLING RESEARCH MANAGER SHIPPELHOUTE: Mr.

8 Gruebele, on page 5 of your testimony you talk about the
9 responsibility of the producer to serve the Class 1
10 market. And you indicate that the producer has that
11 obligation to serve at the Class 1 price plus a reasonable
12 service charge. That differs considerably from Dr.
13 Schiek's testimony earlier that the announced class prices
14 should be sufficient to attract a Class 1 market.

15 Could you perhaps speak to the difference in
16 opinion between yourself and Mr. Schiek.

17 MR. GRUEBELE: Well, I think that -- there are
18 certain services that are being rendered. I think it's a
19 matter of definition of what is reasonable and what is
20 unreasonable as far as premiums are concerned. And I
21 think that may be Dr. Schiek's point, that there are
22 services that are being rendered by plants -- that supply
23 plants, and there should -- you know, a reasonable service
24 charge should be rendered in that particular case. I'm
25 not sure that Dr. Schiek would disagree with that as long

1 as that's reasonable and not unreasonable and we have a
2 pure premium. I think it's a question of whether it's a
3 pure premium or whether it's for services rendered.

4 MILK POOLING RESEARCH MANAGER SHIPPELHOUTE: So
5 you intend to buy service charges -- services provided to
6 your customer for tailoring some of the milk that you
7 supply them?

8 MR. GRUEBELE: That would be an example, yes,
9 sir.

10 DAIRY MARKETING BRANCH ACTING CHIEF ERBA: I have
11 one follow-up question. I should have made a note here,
12 and I forgot. That's why you kind of left me hanging
13 there in your response.

14 Would it be easier or better to do something with
15 the mileage brackets to deal with the high desert
16 producers rather than try to set up a separate rate
17 structure for particular counties?

18 MR. GRUEBELE: It happens that I think that there
19 are -- most of the producers, as I understand it -- and we
20 don't -- they're not our producers, so I had to get
21 information from the firm that those producers belong to.

22 It is my understanding that most of the mileage
23 bracket is covered between 89 and the 134 -- the 139.
24 There was a year ago one producer that was located more
25 than 89 miles from the market. And I don't know that to

1 be the case currently, because I was not able to obtain
2 that information.

3 But I'm not sure how you would do it since those
4 producers are also located between 89 and 139 miles, what
5 mileage bracket we would want to select to correct that
6 problem. I would have to defer to the firm that has those
7 producers and that market to see whether something else
8 could be done. And I would be willing to do so in the
9 post-hearing brief make some comments if that's relevant,
10 if some other method could be -- if some other procedure
11 could be used to accommodate that particular situation.

12 DAIRY MARKETING BRANCH ACTING CHIEF ERBA: That
13 would be terrific if you could do that. Thank you.

14 MR. GRUEBELE: Thanks.

15 HEARING OFFICER ESTES: Is the panel concluded
16 with the questioning?

17 All right. Well, thank you for your testimony
18 today.

19 The last alternative petition today is for
20 Security Milk producers Association.

21 Do you swear or affirm to tell the truth and
22 nothing but the truth today?

23 MR. PERKINS: I do.

24 HEARING OFFICER ESTES: Could you please state
25 your name and spell your last name for the record.

1 MR. PERKINS: Hank Perkins P-e-r-k-i-n-s.

2 HEARING OFFICER ESTES: And could you please
3 explain how you've been authorized to appear and testify
4 on behalf of Security Milk Producers Association today?

5 MR. PERKINS: The Security Milk Producers
6 Association Board of Directors has approved me to testify
7 today in their July 14th meeting.

8 HEARING OFFICER ESTES: I see.

9 You've passed out a written statement. Would you
10 like that introduced into the record today?

11 MR. PERKINS: Yes, I would.

12 HEARING OFFICER ESTES: It will be introduced
13 into the record as Exhibit No. 51.

14 (Thereupon the above-referred to document
15 was marked by the hearing officer as
16 Exhibit 51.)

17 HEARING OFFICER ESTES: So please proceed with
18 your testimony.

19 MR. PERKINS: Mr. Hearing Officer and members of
20 the panel. My name's Hank Perkins. And I'm here today
21 representing Security Milk Producers Association, a
22 cooperative of dairymen in California, Arizona and Nevada.

23 The Board of directors for SMPA approved this
24 testimony at their July 14th, 2004, meeting. We would
25 like to thank the Department for calling this hearing to

1 address the serious situation facing California producers
2 regarding high fuel and energy costs and equitable
3 transportation allowances. At this time SMPA respectfully
4 submits its testimony in these areas.

5 Pooling Plans for Market Milk Section 921.2(e):

6 Today's market transportation costs have climbed
7 in all areas. This fact is supported by the attached
8 comparison of hauling rates prepared by the Dairy
9 Marketing Branch of CDFA. The most recent data through
10 April 2004 indicates increased hauling rates in all areas.
11 Fuel surcharges are a major factor as they now average
12 approximately 12 percent.

13 According to the survey, a dairyman in Tulare
14 ships milk to a Class 1 plant in Los Angeles and has an
15 average haul rate of .972 per hundredweight. The current
16 system pays that dairyman 58 cents per hundredweight
17 transportation allowance, an amount that hasn't changed
18 since 1994. Giving an effective cost of .972 minus the 58
19 equals .392 per hundredweight to supply milk to a bottling
20 plant in Los Angeles from Tulare County. The current
21 local competitive rate shown in CDFA's comparison is .254
22 per hundredweight. The 392 minus the 254 equals 13.8
23 cents per hundredweight shortfall.

24 To further emphasize the situation, today's
25 transportation is barely able to meet all of the demands.

1 Therefore the hauling costs seen by SMPA have been closer
2 to a dollar one per hundredweight, yielding a shortfall of
3 .176 per hundredweight, supported by attached hauling
4 invoices from various SMPA carriers.

5 CDFA's comparison also indicates a haul rate of
6 .737 per hundredweight for Kern County to Los Angeles. A
7 Kern County dairyman would receive a transportation
8 allowance of .43 per hundredweight, leaving an effective
9 cost of .307 per hundredweight. In comparison to the
10 local rate there is again a shortfall of .053 per
11 hundredweight.

12 Currently, approximately 55 percent of the milk
13 delivered in southern California comes from over 100 miles
14 away and receives a transportation allowance. Forty loads
15 per day lose .176 per hundredweight, a total of \$109,120
16 in a month. Another 86 loads per day lose .053 per
17 hundredweight or \$70,649 per month. A total of \$179,769
18 loss on freight per month to supply the southern
19 California market.

20 Another major concern is that the current 55
21 percent of supply is increasing rapidly. The balance of
22 production to population is slipping as dairies are
23 replaced by homes. Just another reason that limiting
24 allowances to below 139 miles is unrealistic, especially
25 in today's environment with areas such as Kern County that

1 imposes restrictions that will impede growth and drive
2 costs higher. Pollution restrictions on air and water
3 have curtailed new dairy construction in that county
4 already and the battle continues, to the extent that it is
5 now known as "unfriendly Kern." How is this supposed to
6 satisfy a burgeoning southern California market that is
7 growing so rapidly?

8 To correct this situation we are requesting to
9 increase the transportation allowances for southern
10 California receiving area to the following amounts:

11 Zero through 89 miles, .09 per hundredweight;
12 over 89 miles through 139 miles, .4775 per hundredweight;
13 over 139 miles, .7475 per hundredweight.

14 While much has been said about the cost of
15 transportation allowances for the southern California
16 (about 75 percent of the monthly total), the fact still
17 remains that agricultural products must move to the
18 market. The fastest growing market is southern
19 California, which is losing one-third of its milk supply
20 that's less than 50 miles away. We need to make to make
21 up the shortfall that's facing producers today to be able
22 to meet the demands of the future.

23 Thank you for the opportunity to present this
24 testimony here today.

25 HEARING OFFICER ESTES: Did you want to have the

1 opportunity to file a post-hearing brief?

2 MR. PERKINS: Yes, we would like that
3 opportunity.

4 HEARING OFFICER ESTES: Please present it to the
5 Department in the time as -- please present it to the
6 Department in a timely manner.

7 MR. PERKINS: Okay.

8 HEARING OFFICER ESTES: Do we have any panel
9 questions?

10 MILK POOLING RESEARCH MANAGER SHIPPELHOUTE:

11 A quick question on the invoice you provided.

12 Is this an independent hauler or is this one of
13 your producers hauling the milk?

14 MR. PERKINS: These are all independent haulers
15 for Security Milk Producers. We provided three of them,
16 one for each of the haulers in the Tulare area.

17 MILK POOLING RESEARCH MANAGER SHIPPELHOUTE: And
18 on one of the invoices I see a fuel charge. Was that
19 charge included in the rate that you used when you were
20 computing your proposed change?

21 MR. PERKINS: Yes, it was.

22 MILK POOLING RESEARCH MANAGER SHIPPELHOUTE: Do
23 you anticipate those fuel charges continuing?

24 MR. PERKINS: Yes, we do.

25 MILK POOLING RESEARCH MANAGER SHIPPELHOUTE: No

1 further questions.

2 DAIRY MARKETING BRANCH ACTING CHIEF ERBA: Hello,
3 Mr. Perkins.

4 I spoke with Dr. Gruebele who represents Land O'
5 Lakes about the problem that's being seen in the high
6 desert producers. Are you able to offer any insight or
7 perspective on that situation?

8 MR. PERKINS: Actually no. We have only one
9 small dairy in there. I don't believe that warrants
10 anything that we would support.

11 DAIRY MARKETING BRANCH ACTING CHIEF ERBA:

12 Probably not.

13 Thank you.

14 MILK POOLING BRANCH CHIEF LEE: Going back to the
15 haul weights and fuel surcharges, Mr. Perkins. How is
16 that usually applied in terms of the bills that you
17 receive? Is there a -- do you get a contract and another
18 contract given to you for approval for --

19 MR. PERKINS: Rates are actually set in advance
20 from our haulers. And there's an adjusted fuel surcharge
21 that we get the chart that we don't go off of from them.
22 And we can supply that in our post-hearing brief if you'd
23 like.

24 MILK POOLING BRANCH CHIEF LEE: Is there a time
25 line as to how long they do apply surcharge that they let

1 you know in advance or is it a surprise or --

2 MR. PERKINS: It's a week-by-week change.

3 MILK POOLING BRANCH CHIEF LEE: Thank you.

4 MILK POOLING RESEARCH MANAGER SHIPPELHOUTE: In
5 your testimony you indicate that the southern California
6 market is growing rapidly. Were you referring to the
7 population growth or the market for Class 1 products?

8 MR. PERKINS: Market for Class 1 products from
9 the valley.

10 MILK POOLING RESEARCH MANAGER SHIPPELHOUTE: From
11 the valley. So not an overall growth of Class 1 market
12 necessarily, but the need to move milk a distance.

13 MR. PERKINS: Correct.

14 MILK POOLING RESEARCH MANAGER SHIPPELHOUTE:
15 Okay.

16 HEARING OFFICER ESTES: Do we have any other
17 panel questions?

18 All right. Thanks for your testimony today.

19 We will now proceed to provide for public
20 comment.

21 As I stated earlier, we have a sign-in sheet in
22 the back of the room. A number of you have already signed
23 it. We'll take people on a first-come-first-served basis
24 in the order in which they have signed on the sign-in
25 list.

1 So if you're interested in testifying today and
2 you haven't signed on the list, please do so.

3 Witnesses shall be given up to 20 minutes to
4 testify, or at least to provide comment.

5 The first person that we have here is Richard
6 Shehadey. Please come forward,

7 Mr. Shehadey, do you swear or affirm to tell the
8 truth and nothing but the truth today?

9 MR. SHEHADEY: I do.

10 HEARING OFFICER ESTES: And could you please
11 state your name and spell your last name for the benefit
12 the hearing.

13 MR. SHEHADEY: I have some copies here that I can
14 give you.

15 HEARING OFFICER ESTES: Go ahead and pass those
16 out, and we'll finish up with swearing you in.

17 MR. SHEHADEY: My name is Richard Shehadey with
18 producers Dairy Foods and Bar 20 Dairy Farms. My name is
19 spelled S-h-e-h-a-d-e-y.

20 HEARING OFFICER ESTES: And could you please
21 describe how you've been authorized to speak on behalf of
22 Producers Dairy and Bar 20 Dairy Farms today?

23 MR. SHEHADEY: I'm the President of Producers
24 Dairy Foods and I authorized it myself.

25 HEARING OFFICER ESTES: All right. I see you

1 have a written statement that you've passed out here.

2 Would you like that introduced in the record?

3 MR. SHEHADEY: Yes, I would.

4 HEARING OFFICER ESTES: It will be introduced
5 into the record as Exhibit No. 52.

6 (Thereupon the above-referred to document
7 was marked, by the hearing officer, as
8 Exhibit 52.)

9 HEARING OFFICER ESTES: And please proceed with
10 your testimony.

11 MR. SHEHADEY: Producers Dairy Foods and Bar 20
12 Dairy Farms is submitting the following to be considered
13 and made a part of the public record for the hearing on
14 August 4th, 2004, regarding a request to alter the Milk
15 Pooling Plan.

16 As the production of milk continues to increase
17 in supply counties and the production of milk continues to
18 decrease in deficit counties, the movement of milk from
19 supply counties to deficit counties continues to increase.
20 This creates an increasing transportation credit and
21 transportation allowance burden on the pool, which equates
22 to decreased net prices paid to the farmer.

23 We estimate the burden borne by the average
24 California dairy farmer, of about a thousand cows, to be
25 approximately \$10,500 a year and increasing. We see this

1 as a significant and excessive cost to the farmer that
2 should be borne by the marketplace. The reference section
3 there is 61802(h).

4 Further, with respect to the inequities of the
5 current transportation allowance structure, is the causing
6 of destructive trade practices, not encouraging the
7 intelligent production and orderly marketing of
8 commodities, and creating economic waste. So far today
9 I've not heard anyone talk about economic waste. But it
10 is cited in Section 61802(e) and 62701.

11 This is occurring in two ways: Farmer subsidized
12 milk from surplus counties is being processed and packaged
13 in deficit counties and then shipped back into surplus
14 counties. This is also increasing rates. An example of
15 this are major processors in the Bay Area, a deficit area,
16 hauling finished products back to the valley, a surplus
17 area, to service customers such as Wal Marts, Winco Foods,
18 Right Aid Drug Stores, Walgreens, Longs, and Whole Food
19 stores, just to name a few, with milk that has been
20 sourced in the valley, and the haul was subsidized by the
21 producers.

22 Number 2, handlers processing and packaging milk
23 in surplus counties and shipping into these deficit
24 counties receive no subsidy for hauling milk into the
25 deficit counties, and are therefore at a competitive

1 disadvantage in those market places. This actually
2 creates an economic incentive for handlers to move their
3 operations into deficit counties in order to obtain the
4 subsidized transportation costs and have the pool and the
5 farmer pay for it.

6 Therefore, we propose the following options as
7 alternative proposals for consideration:

8 1) Milk that is received in deficit counties
9 should not receive a transportation allowance for the
10 portion of milk that's moved back into the surplus
11 counties as finished packaged milk.

12 2) Milk that is packaged in surplus counties and
13 moved into deficit counties as finished packaged milk
14 should be given a transportation credit equivalent to the
15 transportation allowance given for raw milk movement
16 between the two respective areas to encourage movement of
17 milk to the deficit counties.

18 3) While proposal 2 would encourage the
19 intelligent production and orderly marketing of
20 commodities, it would require an increasing burden on the
21 pool.

22 Therefore, an alternate proposal to this would
23 result in the same benefit but actually reduce the cost to
24 the pool, and that would be the discontinuance of
25 transportation allowance and transportation credit

1 programs, thereby allowing the market to decide through
2 the nature of supply and demand. Given the current market
3 conditions and the inequities of the system to both
4 farmers and handlers, we believe that this option is the
5 most consistent with the requirements of section 61802(e)
6 and (h).

7 4) While proposal 3 above is most consistent with
8 current market conditions, an alternate proposal, which
9 would be number 4 here, is to transition from a
10 transportation allowance program to a market order
11 program, whereas orders are established similar to the
12 federal Class 1 price structure shown on the attached
13 published map that was issued by the Pooling Bureau, I
14 believe. And price differentials are defined per area.
15 If you reference 61805(b), it gives you the authority to
16 do this. This would also encourage higher Class 1 milk to
17 move to the deficit marketplace where it belongs.

18 That concludes my written testimony. And I have
19 a few other comments that I'd like to make.

20 HEARING OFFICER ESTES: Please proceed with them.

21 MR. SHEHADEY: Thank you.

22 We would like to request the opportunity to send
23 in a post-hearing brief.

24 HEARING OFFICER ESTES: You may certainly do so.

25 Did you hear --

1 MR. SHEHADEY: August 16th at 4:30; that's Monday
2 afternoon.

3 HEARING OFFICER ESTES: Yes.

4 MR. SHEHADEY: I would like to make a couple of
5 points.

6 One is we don't believe that any area should have
7 a zero mile start. If you look at the reasons for the
8 zero mile start, it shows the inequity in the system
9 throughout the state. And what would the reason be for a
10 zero mile if you don't do it everywhere? I don't
11 understand that -- or we don't understand that.

12 Another point I'd like to make is there was some
13 comment earlier by the Dairy Institute of California. And
14 if you look at their membership, their Class 1 members are
15 all in deficit areas, to my knowledge. And that would be
16 the reason that they would support larger increases in
17 moving the milk to the deficit areas.

18 Another comment I'd like to make is, there's been
19 powerful forces in the industry and they brought about
20 these inequities, at the expense of the producers. And we
21 feel it's time to address and fix them, not keep putting
22 band-aids on them as has been done in the past at these
23 hearings.

24 Supply and demand forces will cause milk to move
25 to the population centers, as the demand is there and

1 they'll pull the milk that direction.

2 Another note. We've not received a "Thank you"
3 letter from the pool or the producers for moving about 65
4 percent of the milk we sell into deficit areas at our own
5 cost.

6 So that concludes my testimony. And I'd like to
7 answer any questions you might have.

8 HEARING OFFICER ESTES: Do we have any panel
9 questions?

10 MILK POOLING RESEARCH MANAGER SHIPPELHOUTE: Mr.
11 Shehadey, just for the record, I just want to clarify that
12 the references to various sections that you make are
13 references to the Food & Ag Code?

14 MR. SHEHADEY: Yes it is. They're attached here,
15 I think it's page 3 and 4. And then the Federal Order
16 Class 1 price structure is attached as about 4, and page 5
17 and 6, the map.

18 MILK POOLING RESEARCH MANAGER SHIPPELHOUTE: You
19 also asked these be considered as alternative proposals.
20 You were aware that there was a deadline for submitting
21 alternative proposals. Formal term -- alternative
22 proposals were due some time ago. So I'm assuming that
23 you would like this considered as oral testimony as
24 opposed to a formal alternative proposal?

25 MR. SHEHADEY: Yes.

1 MILK POOLING RESEARCH MANAGER SHIPPELHOUTE:

2 Could you explain to me how you envision or how
3 you believe adopting an area differential system similar
4 to what they have in the federal order, how that would
5 accomplish the objective that you mentioned?

6 MR. SHEHADEY: Well, one point would be there's a
7 lot of testimony today about out-of-state milk coming into
8 the southern California area. If you look at this map,
9 the southern California area, the heart of it is I guess
10 Los Angeles, is 2.1 -- be \$2.10 I guess the way this
11 federal structure works.

12 If you look at Arizona along the border, it's
13 also 2.1. So they would have the same cost at that point,
14 plus the haul of bringing it into L.A., which would
15 equalize that whole situation that a lot of people seem to
16 be concerned about.

17 The other reason would be to bring it from the
18 valley to the major deficit areas. The differential in
19 price would pay the difference for -- with a shortfall of
20 local haul, it would cover the difference of the cost for
21 hauling. We used to do that up until about 1982, I think.

22 MILK POOLING RESEARCH MANAGER SHIPPELHOUTE: And
23 when you say, "We used to do that," I'm assuming you're
24 referencing the different market areas, at that time there
25 were considerably more market areas?

1 MR. SHEHADEY: There were more market areas,
2 which represented the deficit and surplus areas in a
3 better light.

4 MILK POOLING RESEARCH MANAGER SHIPPELHOUTE: Now,
5 the money that was generated by those different marketing
6 areas, was that not distributed back to the producers
7 equally across the state?

8 MR. SHEHADEY: I believe it was at the plant of
9 receipt.

10 MILK POOLING RESEARCH MANAGER SHIPPELHOUTE: With
11 an operation of the California pool, the plant of first
12 receipt then does pay into the pool based on the location
13 of the -- of that processing plant, but the distribution
14 of the revenue back to the California farmer was -- that
15 is done equally across the state?

16 MR. SHEHADEY: But the processor in that area
17 would pay the farmer what he wants to pay the farmer for
18 the milk he receives.

19 So if you had a plant in a deficit area, paying
20 the higher price into the pool -- I'm just trying to think
21 through this as I go -- by adopting such a system, you're
22 suggesting that there would be some prices paid outside of
23 the pool via the marketplace to the producer, would that
24 generate some unequal raw product costs between handlers
25 that are competing in the same marketplace?

1 MR. SHEHADEY: It shouldn't, because the market
2 area should represent the marketplace. The deficit area
3 should be at a higher price than the surplus areas. So
4 that's supply and demand. If you look at the federal map,
5 that's pretty much what it shows you. That's the concept
6 I'm presenting here.

7 MILK POOLING RESEARCH MANAGER SHIPPELHOUTE: No
8 further questions.

9 DAIRY MARKETING BRANCH ACTING CHIEF ERBA: Hi,
10 Mr. Shehadey.

11 MR. SHEHADEY: Hi.

12 DAIRY MARKETING BRANCH ACTING CHIEF ERBA: I'm
13 looking at your alternative 3 on your second page. And
14 you suggest a discontinuance of the two systems, the
15 allowance system and the credit system.

16 MR. SHEHADEY: Yes.

17 DAIRY MARKETING BRANCH ACTING CHIEF ERBA: And
18 what comes to light when I look at that is: Do you think
19 producers have a responsibility to get milk to move to
20 Class 1 markets?

21 MR. SHEHADEY: That's a hard question to answer.

22 Not necessarily.

23 DAIRY MARKETING BRANCH ACTING CHIEF ERBA: There
24 are lots of ways to get milk to move. It doesn't
25 necessarily need to move by this system. I'm just trying

1 to understand if you think it's not a responsibility the
2 producers to get the milk to that market; is that correct?

3 MR. SHEHADEY: I don't believe so, no.

4 DAIRY MARKETING BRANCH ACTING CHIEF ERBA: Okay.

5 Secondly, you made a comment on the zero mile areas when
6 there's zero mile brackets, that you essentially get --
7 even if you move milk only one mile or less than one mile,
8 you might qualify for some type of allowance, and you
9 suggested that should not exist.

10 MR. SHEHADEY: Yes.

11 DAIRY MARKETING BRANCH ACTING CHIEF ERBA: Do you
12 have an alternative in mind to what system exists now that
13 does have a zero-mile starts?

14 MR. SHEHADEY: I think it should -- if you're
15 going to have a zero mile, it should be throughout the
16 state, so that every processor has the same advantage or
17 disadvantage.

18 DAIRY MARKETING BRANCH ACTING CHIEF ERBA: So
19 would that apply to every handler no matter where they're
20 located or --

21 MR. SHEHADEY: Yes.

22 DAIRY MARKETING BRANCH ACTING CHIEF ERBA:

23 -- only ones that are in the approved receiving
24 areas now?

25 MR. SHEHADEY: No, it should be all throughout

1 the state with every handler.

2 DAIRY MARKETING BRANCH ACTING CHIEF ERBA: Okay.

3 Thank you.

4 HEARING OFFICER ESTES: Do we have any more panel
5 questions?

6 DAIRY MARKETING BRANCH CHIEF IKARI: Just one
7 question.

8 You mentioned the deficit versus the supply. How
9 much of the Class 1 sales are produced in the deficit
10 areas --

11 MR. SHEHADEY: I don't know.

12 DAIRY MARKETING BRANCH CHIEF IKARI:

13 -- processed?

14 MR. SHEHADEY: Most of it.

15 Class 1 milk?

16 DAIRY MARKETING BRANCH CHIEF IKARI: Yes.

17 MR. SHEHADEY: Most of it.

18 DAIRY MARKETING BRANCH CHIEF IKARI: Most of the
19 state's Class 1 milk is processed in the deficit areas?

20 MR. SHEHADEY: I would say that, southern
21 California and the Bay Area.

22 DAIRY MARKETING BRANCH CHIEF IKARI: Okay. And
23 then that's where the greatest portion of the consumption
24 takes place in California?

25 MR. SHEHADEY: I would think so. That's where

1 the population is.

2 DAIRY MARKETING BRANCH CHIEF IKARI: Okay. Thank
3 you.

4 HEARING OFFICER ESTES: All right. Is the panel
5 finished with the witness?

6 DAIRY MARKETING BRANCH ACTING CHIEF ERBA: Yes.

7 HEARING OFFICER ESTES: All right. Thank you for
8 your appearance today.

9 DAIRY MARKETING BRANCH CHIEF IKARI: Thank you.

10 MR. SHEHADEY: Thank you.

11 HEARING OFFICER ESTES: And you've already talked
12 about the post-hearing brief.

13 Okay. Our next witness today is Kevin Abernathy
14 of the California Dairy Campaign.

15 If Mr. Abernathy would come forward.

16 Mr. Abernathy, before I take you on your --
17 before I swear you in today. We have about -- I believe
18 we have like about four or five more witnesses for
19 comment. It's my inclination to conclude with the
20 testimony and not take a lunch break, unless the panel has
21 an objection to that procedure.

22 So we will be trying to conclude the hearing as
23 expeditiously as possible. I believe that some of the
24 staff may also have some afternoon obligations, which it
25 might help facilitate them to fill them if we also

1 proceeded through lunch with this hearing. So that's
2 my -- just so the audience is aware, we will go ahead and
3 take testimony until the hearing is concluded.

4 Mr. Abernathy, do you swear or affirm to tell the
5 truth and nothing but the truth?

6 MR. ABERNATHY: Yes.

7 HEARING OFFICER ESTES: And could you please
8 state your name and spell last name for the record.

9 MR. ABERNATHY: Kevin Abernathy
10 A-b-e-r-n-a-t-h-y.

11 HEARING OFFICER ESTES: And could you -- you're
12 here testifying on -- could you please describe on whose
13 behalf you're testifying and how you are authorized to do
14 so.

15 MR. ABERNATHY: I'm testifying on behalf of the
16 California Dairy Campaign, which I've been authorized
17 through CDC's Board on approval of their position as of
18 July 28th, 2004.

19 HEARING OFFICER ESTES: And you've handed the
20 panel and myself a written statement. Would you like it
21 introduced into the record?

22 MR. ABERNATHY: Yes.

23 HEARING OFFICER ESTES: That will be introduced
24 into the record as Exhibit No. 53.

25 (Thereupon the above-referred to document

1 was marked, by the hearing officer, as
2 Exhibit 53.)

3 HEARING OFFICER ESTES: And please proceed with
4 your testimony.

5 MR. ABERNATHY: On behalf of the California Dairy
6 Campaign, we appreciate the opportunity to testify before
7 the California Department of Food and Ag today. CDC
8 represents more than 350 dairy farmers throughout the
9 State of California. The California Dairy Campaign Board
10 of Directors approved CDC's position at the July 28, 2004,
11 board meeting.

12 CDC testifies today in opposition to all of the
13 petitions to adjust the transportation allowances and
14 credits. We do not believe that the proposals to increase
15 the transportation allowances are necessary and question
16 the need for any allowances or credits. We consider it to
17 be fundamentally unfair that the dairy producer is
18 required to pay additional transportation costs when milk
19 is marketed.

20 The transportation allowances provide a false
21 incentive for milk shipments to certain parts of the
22 state. And the current transportation allowances and
23 credits prevent the efficiency of marketing milk and,
24 instead, foster a milk movement system that is not market
25 oriented. And I think this is prevalent today as to some

1 of the testimony.

2 A recently released Consumer Union report titled
3 "Getting Milked" documented the tremendous profit that
4 retailers are reaping under the current milk pricing
5 system. The Consumers Union survey calculated the wide
6 gap between the price that farmers are paid for milk and
7 the retail price that consumers are paying in the Bay Area
8 of California.

9 In that report the farm-to-retail price
10 differential ranged from \$2.89 to \$3.59 per gallon, or 152
11 to 241 percent profit. Given the tremendous opportunity
12 on Class 1 milk sales, we do not believe that dairy
13 producers should be required to stabilize milk movements
14 throughout the state.

15 In preparation for our testimony today we
16 conducted a survey of hauling rates throughout various
17 areas of the state. And from our survey we found that
18 typical the hauling rates, for one area, for example, of
19 Tulare to Los Angeles, averaged approximately \$435, or 87
20 cents per a 50,000-pound load. Which that maximum load is
21 somewhat lower than what the average gross load would be
22 based on the vehicles today tare weights. That calculates
23 out to approximately \$2.18 a mile.

24 However, the CDFA estimate is 98 cents from
25 Tulare to Los Angeles. Overall haul rates shown in the

1 CDFA tables are somewhat higher than the rates that we
2 recorded in our survey. We're concerned about any hauling
3 estimates that are provided by processor entities because
4 under the current system they may have considerable
5 incentive to inflate hauling charges.

6 Before any decision is made by the CDFA
7 pertaining to transportation allowances, we would implore
8 that the Department conduct a more accurate survey of the
9 actual hauling costs. And we encourage the CDFA officials
10 to contact a range of haulers directly to gather more
11 accurate data of actual hauling rates in the State of
12 California.

13 In conclusion of the oral testimony, we testify
14 in opposition of all the petitions pertaining to
15 adjustments in transportation allowances and credits. We
16 appreciate the opportunity to testify today and look
17 forward to continuing to work with the CDFA.

18 That concludes my testimony that was given to you
19 gentlemen. If you have any further questions, I would
20 like to answer those.

21 And also -- go ahead.

22 HEARING OFFICER ESTES: Did you want the
23 opportunity to file a post-hearing brief?

24 MR. ABERNATHY: Yes.

25 And on a verbal side of the coin. When I did

1 some calculations based on the proposed credits and
2 allowances that are allowed -- and I broke it down into a
3 per mileage basis -- what we basically got here is
4 transportation costs that are dead -- cost rates, or pay
5 hauling rates you might say, where you're actually charged
6 a rate one way considering no backhauls. And there's no
7 data to support the inequities or the inefficiencies of
8 the logistics of these transportation companies that are
9 hauling the milk.

10 For example, if I have a ranch-to-plant shipment
11 and I'm coming in at a certain rate, it's that
12 dispatcher's job to decrease or minimize the deadhead
13 mileage from the next point of load to the next point of
14 shipment.

15 So, for example, ranch to plant and then I reload
16 at the plant and do another plant to plant, that
17 transportation company is maximizing his mileage or
18 dollars per mile. And there's no reference in any of the
19 testimony today to actually show just how efficient those
20 transportation companies are being. So we would ask that
21 the CDFA would take a look at the efficiencies of the
22 logistics these companies are implementing as pertaining
23 to the cost that the producers are bearing in
24 transportation credits and allowances.

25 HEARING OFFICER ESTES: Okay. Your request for a

1 post hearing brief is granted.

2 MR. ABERNATHY: Thank you.

3 HEARING OFFICER ESTES: Does the panel have any
4 questions for the witness?

5 DAIRY MARKETING BRANCH CHIEF IKARI: Mr.
6 Abernathy, I wondered if you could in your post-hearing
7 brief submit a description, an explanation of the
8 methodology you used to do the survey of haulers, who you
9 contacted, which firms, what was included in the surveys.
10 Was it firms -- processing firms, hauling firms, and what
11 was the nature of the rates that you received?

12 MR. ABERNATHY: It was hauling firms.

13 DAIRY MARKETING BRANCH CHIEF IKARI: Okay. The
14 Second question is: Does CDC support the pooling program?

15 MR. ABERNATHY: We support -- I think this
16 concept, yes, we would support the pooling program. But
17 some of the inequities that have been created through some
18 of the loopholes, no, we do not support it.

19 DAIRY MARKETING BRANCH CHIEF IKARI: You
20 support --

21 MR. ABERNATHY: I guess the best way that I could
22 explain that is, the retail side of the marketplace,
23 supply and demand, is a much better representation of
24 disbursing costs. In other words, producers -- I mean
25 this is the only industry that I know of that actually

1 produces a product and then pays to have that product
2 processed and shipped. The only industry that I know of.

3 DAIRY MARKETING BRANCH CHIEF IKARI: How many
4 industries do you know that have a program that shares
5 revenues among producers, which is essentially the pooling
6 program?

7 MR. ABERNATHY: Correct.

8 DAIRY MARKETING BRANCH CHIEF IKARI: And what
9 relationship does the pooling program have with the retail
10 prices of dairy products?

11 MR. ABERNATHY: There seems not to be much of
12 anything.

13 DAIRY MARKETING BRANCH CHIEF IKARI: So if you
14 have a pooling program and the revenues are shared, what
15 incentives are there for producers to ship milk to the
16 higher usages? Isn't the incentive that you go to the
17 local -- the plant closest to them? If that's a cheese
18 plant, isn't that where they want to ship?

19 So then how does the producers share the revenues
20 of a higher class of revenues if no milk is going to those
21 plants?

22 MR. ABERNATHY: I'm really not prepared to answer
23 that question. If you would like --

24 DAIRY MARKETING BRANCH CHIEF IKARI: Some of your
25 testimony gets into these fundamental questions.

1 Thank you.

2 MR. ABERNATHY: Would you like that submitted in
3 a post-hearing brief?

4 DAIRY MARKETING BRANCH CHIEF IKARI: If you
5 would -- if you're interested in doing that, please.

6 MR. ABERNATHY: Can you ask the question one more
7 time so I can write it down?

8 DAIRY MARKETING BRANCH CHIEF IKARI: Well, it
9 will be on the hearing record. And then we'll just...

10 HEARING OFFICER ESTES: Do we have any additional
11 questions?

12 MILK POOLING RESEARCH MANAGER SHIPPELHOUTE: Yes,
13 I do, Mr. Abernathy.

14 In your post-hearing brief, if you can also
15 address your statement here that the transportation
16 allowance provides a false incentive for milk shipments to
17 certain parts of the state. I'd be interested in seeing
18 what parts of the state should not be receiving the milk
19 that it is today and how the allowances are providing a
20 false incentive to get it there.

21 And also if you could address how the current
22 system prevents the efficient marketing of milk.

23 MR. ABERNATHY: How the current system --

24 MILK POOLING RESEARCH MANAGER SHIPPELHOUTE: How
25 the current transportation allowances and credits prevent

1 the efficient marketing of milk, as you have in your
2 testimony. Perhaps explain the thought that went behind
3 that statement. As Mr. Ikari pointed out, those
4 statements go to some fairly broad policy decisions.
5 They're easy statements to put out there in a short
6 sentence. But it would be interesting for us making
7 policy to know what the thought process was and the
8 justification for those statements.

9 MR. ABERNATHY: Sure.

10 MILK POOLING RESEARCH MANAGER SHIPPELHOUTE: No
11 further questions.

12 MR. ABERNATHY: Thank you.

13 DAIRY MARKETING BRANCH ACTING CHIEF ERBA: Hi,
14 Mr. Abernathy.

15 I don't usually like to ask participants the same
16 question. But in this case I think I will, just because
17 I'm curious about your response. I asked Mr. Shehadey if
18 he thought that producers had a responsibility to pay for
19 the cost of getting milk to Class 1 plants. And in your
20 opinion do they or do they not have that responsibility?

21 MR. ABERNATHY: Can I answer two-fold?

22 DAIRY MARKETING BRANCH ACTING CHIEF ERBA:
23 Absolutely.

24 MR. ABERNATHY: I think on the premise, no. I
25 think, again, we have a much better mechanism to bear the

1 cost after we have processed the product and it goes to
2 the marketplace; to bear the cost at that level rather
3 than the producer level where there's absolutely zero cost
4 of production built into any pricing structure that we're
5 currently under. Thus, showing some of the inequities of
6 the system.

7 I mean there's -- dairymen have only one option
8 and, that is, to be a good businessman and to control
9 costs and expenses from check to check, with no cost of
10 production built in outside of the fact that they're being
11 a good business person.

12 DAIRY MARKETING BRANCH ACTING CHIEF ERBA: Let me
13 follow up with another question. And really just a
14 clarification question on your testimony.

15 You testified you're opposed to the petitions
16 that have been submitted. I understand that. Then you go
17 further to say that you don't believe that the proposals
18 would increase allowances and credits and you question the
19 need for them. Is it your testimony that we should
20 abolish this system as the previous witness has testified?

21 MR. ABERNATHY: Again two-fold. If we
22 continually perpetuate the same thing, yes. But I guess
23 my statement is more to the fact that most of the
24 alternative proposals are trying to increase the
25 transportation allowances and credits. And based on the

1 study or survey that we did, we found that the CDFA's
2 current allowances and credits are well within tolerances
3 that other segments of the transportation industry are
4 currently applying on their transportation rates.

5 So it's not you guys -- CDFA is not way off
6 course in the current allowances and credits that you
7 actually have. I mean if, for example, a typical haul to
8 L.A. was a dollar seven-five a mile, and you guys on your
9 transportation credits and allowances were a dollar
10 twenty-five, yes, that would be an inequity. I did not
11 find that.

12 DAIRY MARKETING BRANCH ACTING CHIEF ERBA: Okay.
13 Thank you.

14 MILK POOLING BRANCH CHIEF LEE: I have a question
15 of Mr. Abernathy.

16 You mentioned the tremendous profits that are
17 being earned by retailers from milk that they sell. How
18 would you -- well, let me ask you this: Would you in
19 terms of changing the system -- or to that effect, how
20 would you want those profits being reflected in the
21 producer pricing system?

22 MR. ABERNATHY: I didn't quite --

23 MILK POOLING BRANCH CHIEF LEE: Well, you
24 mentioned that there's, you know, lots of -- tremendous
25 profits being earned at the retail level. And I'm -- are

1 you assuming by your comments that producers should reap
2 some of those profits?

3 MR. ABERNATHY: I would like to see a little more
4 fair and equitable system. I think it was back in the
5 mid-eighties when the parity system was disbanded when
6 consumer prices and farm prices pretty well followed the
7 same track on a graph. And when that program was done
8 away with, we saw a huge separation of those two lines
9 that used to be pretty well parallel.

10 So I would say that we would -- we would
11 definitely like to see something that, number one, keeps a
12 high quality food source in the consumer's hands, but at
13 the same time offers the ability for the people producing
14 that product a fair and equitable lifestyle.

15 MILK POOLING BRANCH CHIEF LEE: Thank you.

16 DAIRY MARKETING BRANCH CHIEF IKARI: One other
17 question for clarification. I didn't catch it the first
18 time. And perhaps you can clarify this for me.

19 So when you -- in your third paragraph, when you
20 raise the retail price and you talk about the disparity
21 between that high price and the profit from the
22 farm-to-retail price, you're equating the transportation
23 allowances and credits and the request to increase those
24 with that inequity -- the inequity of their high retail
25 prices?

1 MR. ABERNATHY: To me that's kind of comparing
2 apples to oranges.

3 DAIRY MARKETING BRANCH CHIEF IKARI: That's what
4 I thought. I want to make sure I understand. What are
5 you trying to say in that third paragraph?

6 MR. ABERNATHY: What I'm trying to show here is
7 somewhat what Mr. Shehadey had brought up, that from the
8 manufacturing plant to the retail stores to the consumer
9 hands is an area where there's a huge amount of profit to
10 be made especially from the retail source to the consumer.
11 That seems to be a better area to pass on the costs of
12 production, i.e., transportation credits, allowance, fuel
13 surcharges, than back out of the producer's pocket. So
14 based on -- I think the August Class 1 price, I think it
15 was --

16 DAIRY MARKETING BRANCH CHIEF IKARI: So you are
17 relating transportation costs, or the cost to haul the
18 milk to the plant, to the retail price?

19 MR. ABERNATHY: No.

20 DAIRY MARKETING BRANCH CHIEF IKARI: You're not?

21 MR. ABERNATHY: No.

22 DAIRY MARKETING BRANCH CHIEF IKARI: To the
23 margin of the retail -- to the margins that retailers are
24 experiencing when they sell dairy products?

25 MR. ABERNATHY: Well, for example, August Class 1

1 was fifteen thirty-seven at the farm a hundredweight.

2 DAIRY MARKETING BRANCH CHIEF IKARI: Right.

3 MR. ABERNATHY: That same hundredweight at the
4 store at an average four fifty-nine a gallon was \$53.37.
5 The farmer got \$15.37, the retailer got \$53.37. That's 38
6 bucks.

7 DAIRY MARKETING BRANCH CHIEF IKARI: Okay.

8 MR. ABERNATHY: That's the point I was trying to
9 make.

10 DAIRY MARKETING BRANCH CHIEF IKARI: So as long
11 as they're getting that kind of margin, it's not fair for
12 producers to pay for increased transportation allowances?

13 MR. ABERNATHY: Thank you.

14 DAIRY MARKETING BRANCH CHIEF IKARI: That's your
15 point. Okay.

16 MILK POOLING RESEARCH MANAGER SHIPPELHOUTE: Your
17 comments on the hauling survey, you indicated you
18 contacted haulers. I'm assuming it was milk haulers that
19 you contacted?

20 MR. ABERNATHY: Actually a little bit of
21 everything. So let me clarify that.

22 In transportation specialized hauling is
23 specialized hauling, whether it would be transportation of
24 milk, hazardous materials, car haulers, enclosed
25 containers, temperature control. I mean all their rates

1 are somewhat similar on a per-mileage basis.

2 The difference is when you start -- which there
3 was nothing in even the workshop that talked about
4 demerged rates, you know, what are the contracts that are
5 being contracted between the processor and the shipper or
6 the hauling company as far as, you know, demerged time for
7 load and unload; none of that was discussed. Nor do we
8 know who was preparing this.

9 MILK POOLING RESEARCH MANAGER SHIPPELHOUTE: Do
10 you know how the CDFA accumulates the data that we publish
11 in our hauling survey?

12 MR. ABERNATHY: I'm learning.

13 MILK POOLING RESEARCH MANAGER SHIPPELHOUTE:

14 Well, you have indicated that you would like the
15 Department to conduct a more accurate survey. And I'm
16 just kind of curious if you had some suggestions on how we
17 may better do that at this time --

18 MR. ABERNATHY: -- is the contracts between
19 Company X and Processor X, is that public knowledge to
20 you, CDFA? And if it's not, it should be, because that's
21 the only true way to make the transportation credits and
22 allowances work concurrently together but not create any
23 sort of inequities in the system itself. If I had the
24 ability that I know that based on your published rates of
25 25.25 cents and I contract with a shipper at 23.25 cents,

1 I now have the ability to make a couple cents per
2 hundredweight. That's an inequity. That's what I was --
3 that's exactly what I was talking about when I mentioned
4 inequities on that level.

5 MILK POOLING RESEARCH MANAGER SHIPPELHOUTE: So
6 if we were able to obtain the actual rates that the plants
7 are invoiced by the hauler and publish those numbers, you
8 would be comfortable with those?

9 MR. ABERNATHY: I think we would have to be, yes.

10 MILK POOLING RESEARCH MANAGER SHIPPELHOUTE:

11 Okay.

12 HEARING OFFICER ESTES: Okay. Is the panel
13 concluded?

14 All right. Thank you for your appearance today.

15 MR. ABERNATHY: Thank you.

16 HEARING OFFICER ESTES: The next witness is
17 Tiffany LaMendola of Western United Dairymen.

18 Ms. LaMendola, would you please -- do you swear
19 or affirm to tell the truth and nothing but the truth
20 today?

21 MS. LaMENDOLA: I do.

22 HEARING OFFICER ESTES: And could you please
23 state your name and spell your last name for the hearing
24 reporter.

25 MS. LaMENDOLA: Tiffany LaMendola

1 L-a-M-e-n-d-o-l-a.

2 HEARING OFFICER ESTES: And would you please
3 describe how you've been authorized to speak on behalf of
4 the Western United Dairymen today?

5 MS. LaMENDOLA: Our board of director's approved
6 my testimony.

7 HEARING OFFICER ESTES: And would you like your
8 written statements introduced into the record today?

9 MS. LaMENDOLA: Yes, please.

10 HEARING OFFICER ESTES: It will be introduced
11 into the record as Exhibit No. 54.

12 (Thereupon the above-referred to document
13 was marked, by the hearing officer, as
14 Exhibit 54.)

15 HEARING OFFICER ESTES: And please proceed with
16 your testimony.

17 MS. LaMENDOLA: Mr. Hearing Officer and members
18 of the hearing panel. My name is Tiffany LaMendola. I am
19 the Director of Economic Analysis for Western United
20 Dairymen. Our association is the largest dairy producer
21 trade association in California, representing a
22 approximately 1100 of the state's dairy families. We are
23 a grass roots organization headquartered in Modesto,
24 California. An elected board of directors governs our
25 policy. The board of directors met July 23rd to approve

1 the position I will present here today.

2 Because we are privy only to aggregated data
3 provided by the Department and are not directly involved
4 with the shipment of milk, our testimony today will
5 generally be limited to policy recommendations. These
6 recommendations are very similar, if not identical, to the
7 positions taken by Western United at the June 4th, 2003,
8 hearing.

9 Basic criteria:

10 Our committee and board both agree with and
11 continue to support guidelines set forth by the Department
12 during the last hearing with respect to setting
13 transportation incentives. I won't repeat those. We
14 strongly encourage the Department to stay committed to
15 these basic tenets in their review of the proposals at
16 hand and in their recommendations to the Secretary.

17 Current system:

18 Upon review of the transportation incentives in
19 preparation for this hearing our board of directors raised
20 many serious concerns. It is apparent there are flaws in
21 the current milk movement system that need to be
22 addressed.

23 However, it is also apparent there are no easy
24 solutions. Additionally, there continue to be looming
25 threats to the California system as well as many dynamic

1 changes occurring in the state. While this hearing does
2 not deal with major changes, it is becoming clear that at
3 some point the industry may need to seriously consider how
4 we can adapt the system to meet current and impending
5 challenges.

6 For instance, data provided at the last hearing
7 by the Department confirmed the fact that southern
8 California has plenty of milk to fill its Class 1 needs,
9 yet producers pay millions of dollars to facilitate
10 movement of more milk into the market.

11 However, evidence suggests that this may be
12 rapidly changing as the southern California milk supply
13 continues its decline. The cost of the transportation
14 incentive program has surpassed 1.7 million in recent
15 months, a cost far in excess of what anybody would like to
16 see. As availability of milk in southern California
17 deteriorates, how will we continue to address the need to
18 supply the Class 1 market yet minimize costs to the pool?

19 Additionally, unregulated out-of-state milk
20 continues to flow in at rapid rates, threatening the
21 stability of the California pool. Given how it is now
22 accounted for in the pool, there is even greater
23 incentives for some plants to purchase out-of-state milk
24 or for round-tripping to reoccur.

25 Good news suggests that some of the southern

1 California market has been recaptured by California
2 cooperatives. However, with the outcome of the lawsuit
3 still pending, how do we address out-of-state threats that
4 exist without greatly increasing the cost of the current
5 system?

6 These are just a few concerns; issues like this
7 are numerous. Though we do not pretend to know all the
8 solutions to these problems, we encourage the Department
9 to keep them in mind as they recommend changes.

10 Petition and alternative proposals:

11 In addition to the basic tenets outlined above,
12 our board was able to come to agreement that a
13 common-sense approach should be used in setting
14 transportation allowances. That is, to the greatest
15 extent possible, allowances should be based on data from
16 the Department. This is the most reliable data available
17 to the industry as a whole.

18 We agree with the basic guiding principle that
19 has historically been used: Through transportation
20 allowances, shippers should be made indifferent when
21 choosing to ship the milk locally or to the more distant,
22 and presumably higher usage, plant. We also agree with
23 the Department that a shortfall should continue to exist
24 in the structure of any area receiving a transportation
25 allowance to encourage the closest milk to move first.

1 Clover Stornetta Petition:

2 We support the addition of Marin and Sonoma
3 counties to the Bay Area receiving area; however, not at
4 the rates requested by Clover Stornetta. According to
5 data released by the Department, it does in fact cost more
6 to ship to the local Class 1 plant than to the Bay Area.
7 However, we have reason to believe that the local haul
8 rate supplied to the Department for the North Bay area may
9 be inflated due to several reasons.

10 These include surcharges, smaller loads in the
11 area, twice-a-day pick-ups, inflated hauling costs for
12 some producers in the area, et cetera. It is our
13 understanding that the core charge hauling rate in the
14 area is approximately 33 cents. This covers the
15 contracted haul rate plus surcharges.

16 We suggest that perhaps the transportation
17 allowance offered for the local haul in the North Bay
18 should be the core charge less approximately 25 cents that
19 should be covered by the producer. This would result in a
20 transportation allowance of around 8 cents.

21 Also, we feel the mileage brackets for the
22 Marin/Somona receiving areas are be limited to two
23 brackets, zero to 40 and 49 plus. It is our understanding
24 that all but one of Clover Stornetta shippers would likely
25 fall into the zero to 49 mileage bracket. The other could

1 be covered under the 49 plus bracket. We do not have
2 enough data available to us to suggest an appropriate rate
3 for the 49 plus bracket.

4 Furthermore, our suggestion for the zero to 49
5 mileage bracket is just an estimate. In both cases we
6 suggest the Department look at the data available to them
7 to set the appropriate rates. Our suggestions here would
8 seem to follow the general set-up for the Sacramento
9 receiving area.

10 Dairy Institute Alternative Proposal:

11 We do not support the Dairy Institute's
12 alternative proposal due to the approach we have taken
13 above. Certainly the transportation allowance for the
14 current Bay Area receiving counties should not be reduced.
15 If the Department decides to add Marin/Sonoma counties,
16 they should not do so at the cost of producers currently
17 shipping to the Bay Area. There are no indications that
18 the cost of shipping to the Bay Area have declined.

19 Though the Institute is attempting to make a
20 producer indifferent to shipping locally or long distance,
21 lowering the current allowance would leave producers
22 supplying the Class 1 market in the Bay Area with a
23 shortfall and not guarantee them an alternative outlet for
24 their milk. The Clover Stornetta demand for milk is
25 limited and could not accommodate all the producers who

1 may wish to switch from shipping to the Bay Area to the
2 local Class 1 plant given a reduction in the allowance.
3 Furthermore, with the closure of the DFA cheese plant,
4 demand for North Bay milk has declined.

5 If the Department chooses to add Marin/Sonoma
6 counties to the Bay Area receiving area, they should not
7 do so at the risk of discouraging producers from shipping
8 to Bay Area Class 1 plants by lowering the available
9 allowance.

10 Land O' Lakes:

11 We cannot support any part of the LOL alternative
12 proposal.

13 The Land O' Lakes' proposal to limit supply
14 counties and reduce allowances for certain counties
15 supplying southern California seems to have two apparent
16 goals: 1) Reduce transportation allowance for producers
17 located in San Bernardino County who, they argue, are
18 receiving higher than necessary allowances; and 2) limit
19 shipments of milk into southern California from certain
20 far out counties.

21 Of particular concern to our board is the fact
22 that the some producers may be overcompensated for their
23 hauling costs through transportation allowances. Under no
24 circumstances should producers make money off
25 transportation allowances. This is not the purpose of the

1 transportation allowances and unnecessarily increases
2 costs to the pool. However, our concern is statewide
3 rather than for any specific county. No matter where a
4 producer is located, they should not make money off
5 transportation allowances.

6 Though we will not comment on LOL's specific
7 proposal to change supply counties and rates for certain
8 counties, we urge the Department to review allowances and
9 respective hauling rates in all areas of the state when
10 making recommendations on changing allowances. If changes
11 need to be made, we urge them to do so in order to
12 minimize costs to the pool.

13 As we stated at the June 4th, 2003, hearing, our
14 board would like to see the southern California market
15 served primarily by closer-in milk. This makes sense.
16 However, for some reason this is not occurring.

17 Therefore, if milk is going to move from further
18 distances, why should the counties be limited? If milk
19 moves from Tulare county at a cost of 58 cents per
20 hundredweight versus from Stanislaus County at a cost of
21 58 cents per hundredweight, there is no difference in the
22 total cost to the pool. Obviously, if the milk would move
23 from a closer location, there could potentially be cost
24 savings involved. However, we have no way of knowing
25 whether or not this will occur.

1 As CDFA pointed out in a previous hearing panel
2 report, it (the panel) is not willing to exclude other
3 counties from the available transportation rate. To do so
4 discriminates against producers who may wish to ship milk
5 into southern California based strictly on the location of
6 their dairies. Furthermore, designating eligible and
7 ineligible counties may actually decrease the supply of
8 milk available to Class 1 plants, a result which does not
9 work toward the principles previously outlined by the
10 panel.

11 Our board agrees. If milk must move to southern
12 California from distant locations in order to serve the
13 Class 1 market, all counties should be eligible.

14 Increase in transportation credits for bulk milk
15 and condensed skim:

16 We do not support an increase in transportation
17 credits as proposed by LOL. According to departmental
18 analysis, at a minimum the LOL petition would increase the
19 cost of transportation credit system approximately 820,000
20 per year, or a 17 percent increase. We do not see
21 justification for this increase.

22 First and foremost, we do not support a
23 transportation credit on condensed skim and therefore
24 cannot support an increase in the rate. We certainly
25 cannot support a rate even higher than the credit offered

1 for bulk milk. Tailored milk shipped to southern
2 California is already covered by transportation credits.
3 We assume this tailored milk also demands a premium in the
4 marketplace. There is no justification for producers to
5 also cover the costs of hauling a manufactured product
6 such as condensed skim to the southern California market.
7 Processors already receive approximately a 21 cent per
8 hundredweight incentive due to the differential.

9 Furthermore, producers already pay a
10 fortification allowance on condensed skim. LOL is now
11 asking producers to also pay additional hauling costs. We
12 have been told that southern California has plenty of
13 condensed skim capacity. There is no justification to
14 cover the costs of hauling to the southern California
15 market.

16 Anecdotal evidence suggests that the
17 transportation credit on condensed skim moving from Tulare
18 lair to southern California has now put this product at a
19 competitive advantage over condensed skim already located
20 in southern California. If so, this goes entirely against
21 the basic tenets of moving the closest milk first and
22 minimizing costs to the pool.

23 Also, data from the Department indicates that
24 there's currently some milk that receives a transportation
25 allowance and then a transportation credit. This is far

1 beyond the original intent of the transportation incentive
2 system developed in California, increases costs to the
3 pool, and was even a concern of the Department in the last
4 hearing report. The Department should carefully review
5 this along with the concern over competition with southern
6 California condensed skim and reconsider whether credit
7 should be offered to condensed skim at all.

8 Finally, LOL's proposal would eliminate any
9 shortfall in the transportation credits to southern
10 California. According to the Department, historically
11 transportation credits offset some of the cost of hauling
12 milk assigned to Class 1 usage from plants in designated
13 supply counties to plants in designated deficit counties.
14 It is our understanding that it will also eliminate the
15 current relationship between transportation allowances and
16 credits from Tulare to southern California.

17 According to material handed out at the
18 pre-hearing workshop for the last hearing, in 2001 based
19 on this approach, the panel recommended and the Secretary
20 implemented an increase in the transportation allowances
21 into southern California, but left the corresponding
22 transportation credit unchanged. This resulted in an
23 unprecedented level in the shortfall for the credit.

24 However, the panel found that by doing so, it
25 would otherwise have favored plant-to-plant movement over

1 ranch-to-plant. The Department's goal was create a level
2 playing field so that the comparative advantages of
3 ranch-to-plant versus plant-to-plant movement would
4 determine which is used.

5 The LOL proposal disregards the Department's
6 attempt to develop a level playing field. At the last
7 hearing, against recommendations of the panel,
8 transportation credits were increased. This alone threw
9 off the level playing field, providing a greater net draw
10 from the pool for milk moving plant to plant than for the
11 same amount of milk moving ranch to plant. We urge the
12 Department to reestablish the level playing field by not
13 allowing a greater draw from the pool for milk moving
14 plant to plant.

15 CDI:

16 With regard to changes in transportation
17 allowances as requested by CDI, we support a change in
18 transportation allowances to reflect the difference
19 between the local and long distance haul with shortfalls
20 existing for further out distances in both the North Bay
21 and southern California regions. Since we do not have
22 access to hauling costs within specific mileage brackets
23 nor information on shipments between specific counties, we
24 cannot comment on the changes requested by CDI.

25 But we encourage the Department to carefully

1 analyze the data available to them to ascertain whether or
2 not any changes need to be made. Increases to the
3 allowances should be made where increased costs warrant.
4 We do however encourage the Department to strongly
5 consider any possible increases in costs, such as diesel
6 fuel, that may have developed since the May 2004 hauling
7 figures were compiled.

8 According to data from the Department, diesel
9 rates spiked in May. This is a trend that may not
10 continue throughout the remainder of the year.
11 Consideration of any recent developments would be in line
12 with the basic tenet to attempt to minimize costs to the
13 pool.

14 We agree that if Alameda and Contra Costa
15 counties are the only two in the current Bay Area
16 receiving areas with Class 1 plants, then the other
17 counties should be eliminated in order to bring the system
18 up to date. We also agree with CDI's proposal for the San
19 Diego receiving area. According to the Department, nearly
20 all the milk moved with transportation allowances is less
21 than 75 miles from the qualifying plant. If data warrants
22 the small increase in the rate, then it should be
23 adjusted.

24 We can support CDI's request for the addition of
25 L.A. County as a designated deficit county for

1 transportation credits due to the fact that we do not
2 support any transportation credits on condensed skim. Our
3 reasoning was fully outlined above. Because bulk and
4 condensed skim were currently offered the same
5 transportation credit, i.e., grouped together, we also
6 cannot support the requested increase in the credit rate
7 for L.A. County.

8 As previously discussed, anecdotal evidence
9 suggests that the transportation credit on condensed skim
10 moving from Tulare to southern California has now put this
11 product at a competitive advantage over the condensed skim
12 already located in southern California. We once again
13 stress our concern that this goes entirely against the
14 basic tenets of moving the closest milk first and
15 minimizing costs to the pool.

16 DFA alternative proposal:

17 This is essentially identical to the first
18 paragraph I read under the CDI proposal. So I won't read
19 you it.

20 Security milk producers alternative proposal:

21 We do not support Security's alternative
22 proposal. The requested increase in transportation
23 allowances for the furthest out bracket goes against the
24 basic principle of encouraging the closest milk to move
25 first. Our board feels there's adequate milk supply from

1 Kern County south to supply the southern California
2 market. A shortfall in this bracket should be maintained.

3 We thank you for the opportunity to testify and
4 request the option to submit a post-hearing brief.

5 HEARING OFFICER ESTES: Your request is granted.

6 Are there panel questions?

7 DAIRY MARKETING BRANCH ACTING CHIEF ERBA: Hello,
8 Ms. LaMendola.

9 I understand that you are proposing an 8 cent
10 transportation allowance in the Bay Area receiving area
11 for the zero to 49 mile bracket?

12 MS. LaMENDOLA: Yeah, we thought the Marin and
13 Sonoma could be handled separately from the current Bay
14 Area receiving area. And it was just an estimate. But we
15 would encourage the Department to look at the data
16 available to them.

17 DAIRY MARKETING BRANCH ACTING CHIEF ERBA: So
18 does this mean you'd like to create a separate receiving
19 area or add to the receiving area that already exists?

20 MS. LaMENDOLA: It would have to be separate
21 because we don't support a decline in the current rates to
22 the Bay Area.

23 DAIRY MARKETING BRANCH ACTING CHIEF ERBA: Okay.
24 You have stated several times you do not support a
25 transportation credit on condensed skim. But I'm not sure

1 I see your reasoning why.

2 Why doesn't your organization support
3 transportation credit on condensed skim?

4 MS. LaMENDOLA: Well, I did outline a few
5 different reasons. One is that we feel there's sufficient
6 capacity already in southern California of condensed skim
7 that would go along with the basic tenet of moving the
8 closest milk first. We also feel like it's a manufactured
9 product, and producers are not required to move
10 manufactured product to supply a Class 1 market when bulk
11 milk is already covered.

12 The producer's already paying fortification
13 allowance on the product, and should not have to pay
14 additional hauling costs.

15 Most of those ideas are outlined on page 5.

16 DAIRY MARKETING BRANCH ACTING CHIEF ERBA:

17 Lastly, on page 6 you comment on the idea of
18 restricting the Bay Area receiving area to just Alameda
19 and Contra Costa counties. And you say that that should
20 be eliminated -- other counties should be eliminated to
21 bring the system up to date. There's another receiving
22 area, Shasta, hasn't been used for years.

23 Should we eliminate that as well?

24 MS. LaMENDOLA: Yeah, I think that would be a
25 problem. It just wasn't in the proposal put forth, so we

1 didn't comment on it. But certainly --

2 DAIRY MARKETING BRANCH ACTING CHIEF ERBA: I'm
3 giving you the chance now to comment on that. Is that
4 something that should be eliminated?

5 MS. LaMENDOLA: Certainly it is not -- yeah, if
6 it's not being used, there would be no problem with
7 eliminating that as well. Let's keep it up to date as
8 possible.

9 DAIRY MARKETING BRANCH ACTING CHIEF ERBA: Okay.
10 Thank you very much.

11 HEARING OFFICER ESTES: Do we have any additional
12 panel questions?

13 DAIRY MARKETING BRANCH CHIEF IKARI: I just have
14 one.

15 Tiffany, on your testimony on Dairy Institute,
16 you seem to oppose their proposal based on the fact that
17 the producers shipping to the Bay Area would have a
18 shortfall. But is that consistent, milk producers in
19 other areas, they have a shortfall by shipping to Class 1?

20 MS. LaMENDOLA: I think it was just -- the
21 approach they took was to try and equalize it so they
22 would -- they had to lower the shipment rate into the Bay
23 Area in order to equalize it with their recommendation for
24 Sonoma and Marin. And we're just saying the Bay Area has
25 a long history of being established. That should be left

1 alone. And if we need to add Sonoma and Marin, we could
2 do so by creating a separate receiving area without
3 adjusting the ones that are already in place. I think
4 there are shortfalls already built into the system that
5 currently exists for the Bay Area receiving area.

6 DAIRY MARKETING BRANCH CHIEF IKARI: But you do
7 support the concept that shortfalls should exist in the
8 steps --

9 MS. LaMENDOLA: Yeah, in the furthest out
10 brackets, absolutely.

11 DAIRY MARKETING BRANCH CHIEF IKARI: What about
12 the closest brackets?

13 MS. LaMENDOLA: I think it's historically been
14 the furthest out brackets have a greater shortfall.

15 DAIRY MARKETING BRANCH CHIEF IKARI: But there
16 can be shortfalls in the local, right?

17 MS. LaMENDOLA: If that's how it's historically
18 been done, I think it should be a difference between the
19 long haul and the local haul. I don't know -- I think
20 different areas have different shortfalls built in in the
21 shipping maintained.

22 DAIRY MARKETING BRANCH CHIEF IKARI: Thank you.

23 HEARING OFFICER ESTES: Thank you for your
24 testimony today.

25 Our next witness is Stephen James with Swiss

1 Dairy.

2 Mr. James, do you swear or affirm to tell the
3 truth and nothing but the truth today?

4 MR. JAMES: I do.

5 HEARING OFFICER ESTES: And could you please
6 state your name and spell your last name for the hearing
7 reporter?

8 MR. JAMES: I'm Stephen James. Last name is J,
9 as in Jupiter --

10 (Laughter.)

11 MR. JAMES: -- a-m-e-s. And I'm President and
12 General Manager of Swiss Dairy in Riverside, California.

13 HEARING OFFICER ESTES: All right. Please
14 proceed with your testimony.

15 MR. JAMES: Well, I'll do my bit to help with the
16 expeditious completion of the hearing. I will be very
17 brief. I don't have a written statement. I am appearing
18 here to support the proposal by CDI. I'd like to echo
19 some of the comments also that I heard earlier in thanking
20 the Secretary and the Department for your responsiveness
21 to economic and competitive conditions and issues that
22 require periodic adjust adjustments in the system's
23 transportation credits and allowances.

24 And as it's already been stated in the previous
25 testimony, that the competitive assault on California

1 fluid milk from an unregulated plant in Arizona makes
2 these adjustments at least in my case at Swiss Dairy even
3 more critical and more urgent to prevent further erosion
4 of the Class 1 market and producer sharing in that pool.

5 I would also like to request the opportunity to
6 submit a post-hearing brief.

7 HEARING OFFICER ESTES: All right. Your
8 post-hearing brief request is granted.

9 Do we have panel questions?

10 DAIRY MARKETING BRANCH ACTING CHIEF ERBA: I have
11 a question of Mr. James.

12 Hello.

13 MR. JAMES: Hello.

14 DAIRY MARKETING BRANCH ACTING CHIEF ERBA: The
15 CDI was opposed to offering transportation credits on
16 condensed skim. They said so at the last hearing and I
17 think they echoed that in today's hearing as well, with
18 the notion that if we continue the idea of having a credit
19 for a condensed skim, that they ought to make -- be some
20 adjustments made.

21 Do you support their testimony to that fully or
22 do you have a different view on it?

23 MR. JAMES: Well, I support the premise that
24 there should be a level playing field. And I think their
25 opposition to it in the last hearing shouldn't stand in

1 the way of their position now of saying that they are in
2 an uncompetitive position regarding condensed skim --

3 DAIRY MARKETING BRANCH ACTING CHIEF ERBA: Thank
4 you.

5 MR. JAMES: -- as it sounds now.

6 DAIRY MARKETING BRANCH ACTING CHIEF ERBA: Thank
7 you.

8 HEARING OFFICER ESTES: Any other questions?

9 All right. Thank for your appearing today.

10 The next witness I think is Bob Feenstra.

11 Mr. Feenstra, do you swear or affirm to tell the
12 truth and nothing but the truth today?

13 MR. FEENSTRA: I do.

14 HEARING OFFICER ESTES: Could you please state
15 your name and spell your name for the hearing reporter.

16 MR. FEENSTRA: Bob Feenstra F-e-e-n-s-t-r-a,
17 Executive Director of the Milk Producers Council based in
18 Ontario, California.

19 HEARING OFFICER ESTES: Please describe how
20 you've been authorized to testify on behalf of the Milk
21 Producers Council today.

22 MR. FEENSTRA: It was approved by the board of
23 directors at their July 26th board meeting of 2004.

24 HEARING OFFICER ESTES: Do you want your written
25 statement introduced in the record?

1 MR. FEENSTRA: I do.

2 HEARING OFFICER ESTES: It will be introduced
3 into the record as Exhibit No. 55.

4 (Thereupon the above-referred to document
5 was marked by the hearing officer as
6 Exhibit 55.)

7 HEARING OFFICER ESTES: And proceed with your
8 testimony.

9 MR. FEENSTRA: Thank you very much. And we would
10 also like to be able to respond in a post-hearing brief.

11 HEARING OFFICER ESTES: Your request is granted.

12 Did you have the opportunity to hear the deadline
13 for the submission of that brief?

14 MR. FEENSTRA: August 17th.

15 HEARING OFFICER ESTES: 16th.

16 MR. FEENSTRA: 16th.

17 Well, it's getting better all the time. In fact,
18 we'll note that.

19 HEARING OFFICER ESTES: Well, we finally got it
20 straight. You probably were hear for the beginning part
21 and not for the latter part of the discussion. That might
22 explain why you think it was the 17th, since I said so.

23 Anyway, 4:30 -- by the close of business, 4:30,
24 on Monday, the 16th.

25 And please proceed with your testimony.

1 MR. FEENSTRA: Thank you.

2 A few comments, Mr. Hearing Officer, before I go
3 with my prepared statement.

4 First of all, in earlier testimony presented
5 today by Producers Dairy from Fresno, I personally want to
6 provide a "thank you" comment for all the milk that that
7 processing plant ships in finished product throughout the
8 State of California. I enjoy that milk every vacation in
9 Lakeport, California, and we drink our share. So thank
10 you for that, Richard, and I mean it sincerely.

11 The other thing is I'm sort of saddened today by
12 the announcement or comment -- as I'm getting older, I get
13 a little hard of hearing. It can't be true that Mr. Erba
14 is going to move on. If that is the case, Dr. Erba, I
15 want to, on behalf of Milk Producers Council, myself and
16 the members I represent, to thank you for all the
17 courtesies you've extended to us over the years, your
18 support and hard work on behalf of the dairy industry.
19 Just know that it goes with a big "thank you" and a lot of
20 respect, and I wish you would reconsider.

21 DAIRY MARKETING BRANCH ACTING CHIEF ERBA: Thank
22 you.

23 MR. FEENSTRA: Mr. Hearing Officer, thank you for
24 allowing Milk Producers Council the opportunity to provide
25 testimony regarding transportation credits. MPC is a

1 dairy service trade association with 175 members located
2 in southern and central California.

3 Geoffrey Vanden Heuvel, board member of MPC and a
4 dairy producer operating in San Bernardino County, wrote
5 the following testimony which outlines the position of
6 Milk Producers Council.

7 First of all, MPC thanks the Department for the
8 decision adopted as a result of a transportation subsidy
9 system hearing held last year to extend a transportation
10 allowance to producers located in southern California who
11 shipped their milk to Class 1 plants in southern
12 California. It is MPC's opinion that this change created
13 a real incentive for producers located closest to the
14 southern California Class 1 market to pursue the fluid
15 milk market. This is exactly the type of positive
16 incentives that our transportation subsidy system should
17 create.

18 As for the petition from Clover Stornetta, after
19 examining the data and listening to the arguments, we have
20 determined that we do not support the request to add Marin
21 and Sonoma counties to the Bay Area receiving area. We do
22 recognize that the August 2003 hauling rate study did seem
23 to indicate some inequities between the hauling rates paid
24 by producers serving the Bay Area Class 1 plants and those
25 serving the local Class 1 plants in the North Bay area.

1 We also noticed some changes in those hauling rates in the
2 updated study.

3 MPC believes the way to address the equity issue
4 among the North Bay producers is not to add a new and
5 unnecessary transportation allowance to the system, but to
6 support the Dairy Institute's proposal of reducing an
7 obvious generous transportation allowance for milk moving
8 from North Bay to the Bay Area receiving area.

9 In regards to the request to raise the
10 transportation allowance rates for Solano county, after
11 evaluating the data, which included the hauling rate study
12 as well as milk production reports from the green sheet,
13 we believe that there is plenty of milk available for the
14 Solano County plant. Since there is no justification for
15 the substantial rate increase that DFA has requested, we
16 oppose the proposal to raise the Solano County receiving
17 area rate.

18 Milk Producers Council has received alternate
19 proposals that seek to make assorted adjustments to the
20 southern California receiving area transportation
21 allowance rates. We have come to the conclusion that the
22 Department needs to go back to the designation of specific
23 supply counties for the southern California receiving
24 area.

25 While we appreciate the Department's policy

1 change some years ago that eliminated supply counties, in
2 practice this change has led to some irrational results.
3 The one we are most familiar with gives a large and costly
4 transportation allowance to producers in the Barstow area
5 for milk moving into the Los Angeles Class 1 market, an
6 allowance which exceeds their hauling rate. This is
7 unnecessary and should not be allowed to continue. MPC
8 also believes that San Diego should be a part of the
9 southern California receiving area and not a separate
10 receiving area.

11 MPC proposes and supports the following
12 adjustments to the transportation allowance system:

13 1) The southern Cal receiving area should
14 consist of the counties Los Angeles, Orange, Riverside,
15 Ventura and San Diego.

16 2) For milk shipped to qualifying plants in
17 southern California receiving area from Santa Barbara,
18 Kern, Kings, Tulare counties the following transportation
19 allowance rates would apply: You'll note them.

20 3) For milk shipped to qualifying plants in
21 southern California from all other counties the following
22 rates would apply: As listed.

23 MPC supports the rate increases proposed by
24 California Dairies, Inc., CDI, for the counties in the
25 southern San Joaquin Valley because of the clear need to

1 attract milk from that area to southern California. Those
2 producers have other alternatives and the cost of moving
3 milk over the Tejon Pass and into urban southern
4 California has increased over the past year. We believe
5 this increase justifies the transportation rate increases
6 proposed by CDI.

7 MPC, however, does not support the request by
8 Security Milk Producers to dramatically increase the "over
9 139 mile" rate. Milk production reports published by the
10 Department clearly demonstrate that there is a large and
11 growing supply of milk located within the 139-mile bracket
12 which makes the Security request unjustified.

13 The Land O' Lakes proposal regarding
14 transportation credits, in our opinion, is totally
15 unjustified, even though we really do like Dr. -- Jim
16 Gruebele. Great guy. The Department analysis, which
17 compares the efficiency of ranch-to-plant with
18 plant-to-plant movement shows that the benefits of the
19 efficiency of plant-to-plant movement accrue to the
20 processing plants. The producers are charged
21 significantly more dollars to facilitate this movement.
22 The Land O' Lakes proposal would only exacerbate this
23 inequity and must be rejected by the Department.

24 Furthermore, the decision to expand the
25 transportation credit to condensed skim from Tulare County

1 to southern California has understandably provoked a
2 request by CDI for the establishment of a transportation
3 credit for condensed skim within southern California.
4 CDI, with justification, claims that they have been put in
5 an unfair position in marketing condensed skim because
6 their competition receives a producer-funded
7 transportation credit that CDI is not able to offer from
8 their southern California condensed plant.

9 Condensed skim is a value-added practice and not
10 a producer milk. The cost of transporting this product
11 should be borne by the market and not by producer
12 subsidies. Therefore MPC respectfully requests that
13 condensed skim be removed as being eligible for
14 transportation credits.

15 In summary, Milk Producers Council believes that
16 the transportation subsidy system does provide a valuable
17 function in facilitating the movement of California
18 producer milk to the fluid market. Periodic adjustments
19 do need to be made to respond to the changing dynamics of
20 the market. The three longstanding criteria of the
21 transportation subsidy system has served the industry
22 well, and they are:

23 1) Producers who serve the Class 1 market ought
24 to be rewarded.

25 2) The closest milk to the market ought to be

1 move first.

2 3) A regulated system ought to attempt to
3 minimize costs to the pool.

4 MPC believes that the positions and proposals we
5 have made are consistent with these criteria and we urge
6 the Department to adopt them.

7 On behalf of the Milk Producers Council and the
8 Board, thank you for your consideration on this issue.

9 Mr. Hearing Officer, what I'd like to do today is
10 that note any questions that the panel may have regarding
11 this presentation that was prepared by Mr. Vanden Heuvel,
12 and we will respond to them appropriately in the
13 post-hearing brief.

14 HEARING OFFICER ESTES: I see. Are you
15 suggesting that you're not capable of responding to
16 certain questions and would like to --

17 MR. FEENSTRA: I'm capable. But I'd prefer for
18 the person who prepared the statement to provide the
19 responses.

20 HEARING OFFICER ESTES: Okay. Well, then we'll
21 have the panel ask you some questions, and you can take
22 note of them.

23 MR. FEENSTRA: That would be good.

24 DAIRY MARKETING BRANCH ACTING CHIEF ERBA: Mr.
25 Feenstra, you're not going to get off quite that easy.

1 First of all, thank you for your kind words on
2 behalf of you and your organization. I appreciate them.

3 I just have one question that perhaps you can
4 pass along to Mr. Vanden Heuvel. And, that is, points out
5 that the Barstow area, the high desert area, the specific
6 area of concern of the transportation allowance system.
7 And other folks had suggested that we do as Mr. Vanden
8 Heuvel has suggested and, that is, by breaking up the
9 supply counties into a higher rate and a lower rate
10 depending on where the county is.

11 I wonder if you might ask him if he might
12 accomplish the same goal of dealing with that high desert
13 area by looking at changing the mileage bracket and not
14 adjusting the counties that are in or out of the supply
15 county with higher or lower areas.

16 MR. FEENSTRA: We'll pass that on.

17 DAIRY MARKETING BRANCH ACTING CHIEF ERBA: Great.
18 Thank you.

19 HEARING OFFICER ESTES: Are there any other
20 questions?

21 All right. Seeing none.

22 Thank you for appearing here today.

23 Our last -- well, our last witness unless someone
24 else signs up is Sharon Hale from Crystal Cream and Butter
25 Company.

1 Ms. Hale, do you swear to tell the truth and
2 nothing but the truth today?

3 MS. HALE: I do.

4 HEARING OFFICER ESTES: And could you please
5 state your name and spell your last name for the record.

6 MS. HALE: Sharon Hale H-a-l-e.

7 HEARING OFFICER ESTES: And you're appearing
8 today on behalf of the Crystal Cream and Butter Company?

9 MS. HALE: I am.

10 HEARING OFFICER ESTES: And how are you
11 authorized to speak for them today?

12 MS. HALE: I'm an executive of the company, and I
13 developed the testimony in concert with the president.

14 HEARING OFFICER ESTES: I see.

15 Would you like your written statement be
16 introduced in the record?

17 MS. HALE: Yes, I would.

18 HEARING OFFICER ESTES: It will be introduced as
19 Exhibit No. 56.

20 (Thereupon the above-referred to document
21 was marked by the hearing officer as
22 Exhibit 56.)

23 HEARING OFFICER ESTES: And please proceed with
24 your testimony for the benefit of the panel.

25 MS. HALE: Mr. Hearing officer and members of the

1 panel. My name is Sharon Hale and I'm Vice President,
2 Dairy Policy and Procurement, for Crystal Cream and Butter
3 Company. Our administrative offices are located at 1013 D
4 Street, Sacramento, California 95814. We currently
5 operate three production facilities in Sacramento.
6 Crystal purchases the majority of its milk from independent
7 dairy farmers but also buys supplemental milk from
8 cooperatives when necessary to satisfy fluctuating market
9 demands.

10 Crystal is a member of the Dairy Institute of
11 California and supports the testimony given earlier by Dr.
12 Schiek.

13 I would like to add our company's perspective on
14 one element included in the call of the hearing, that
15 being transportation allowances for ranch-to-plant
16 shipments of milk in northern California.

17 This are several proposals to adjust
18 transportation allowances within northern California being
19 considered in this hearing, but none are directed at the
20 transportation allowances for milk moving into the
21 Sacramento deficit area. When the hearing was announced
22 we looked at the hauling rates being paid by independent
23 producers under contract with Crystal whose milk moves
24 into our Sacramento plants.

25 While the actual hauling rates had increased, we

1 felt the incentive to continue shipping to Sacramento
2 remained substantially the same. The Department's latest
3 ranch-to-plant hauling rate survey bears this out.

4 Local hauls from Sacramento/San Joaquin were
5 reported as 32 cents per hundredweight in August of 2003,
6 and by April 2004 had moved to 33 cents per hundredweight,
7 a 1 cent per hundredweight increase. Hauling rates for
8 milk from these same two counties that was shipped into
9 the northern San Joaquin Valley for processing changed
10 from 32.2 cents per hundredweight to 32.8 cents per
11 hundredweight over the same time period, for an increase
12 of .006 per hundredweight.

13 While it appears the incentive to supply the
14 Sacramento deficit market has decreased slightly, Crystal
15 did not feel this change to be significant enough at this
16 time to warrant filing an alternative proposal at this
17 hearing.

18 It is unfortunate the Department's hauling rate
19 survey was not available prior to the due date for
20 alternative proposals. In reviewing that information,
21 which was made available just prior to the pre-hearing
22 workshop, we noticed the haul rate for milk moving from
23 the northern San Joaquin Valley to Sacramento has
24 increased by .043 cents per hundredweight. This more
25 sizeable increase appears to have removed what had been a

1 modest incentive to supply milk to the Sacramento deficit
2 market.

3 A table follows below comparing the differences
4 from the August '03 and the April '04 survey information
5 from the Department.

6 The local northern San Joaquin valley haul in '03
7 was listed at 258, in '04 it's at 272. A haul to
8 Sacramento went from 35.4 to 39.7. That left a
9 disincentive to supply of 9.6 cents in '03, changed to '04
10 at 12.5.

11 The current transportation allowance for dairies
12 located over 59 miles is 12 cents. When that number's
13 factored in, the incentive to ship milk to Sacramento in
14 August '03 was 2.4; and it appears in April of '04 to have
15 decreased to a minus half penny.

16 It is difficult to know what impact this
17 situation might have on our ability to attract milk. We
18 realize the aggregated numbers presented by the Department
19 are designed to mask confidential information; and as
20 such, we are prevented from knowing if milk on the
21 northern end of the area entitled "Northern San Joaquin
22 Valley" is accurately represented by the example shown
23 above. It's our view that milk located in this area
24 should logically be targeted as a likely supply for
25 meeting the needs of the Sacramento market, and we are

1 concerned about diminishing the potential for attracting
2 this milk.

3 We do know some organic milk moving into
4 Sacramento for processing may well be traveling from more
5 southern locations within the northern San Joaquin Valley
6 supply area and, therefore, incurring a higher haul rate
7 than the conventional milk which moves to Sacramento.
8 Organic loads also tend to be smaller, which increases the
9 hundredweight cost of moving that milk as well.

10 At this time we are not concerned about trying to
11 provide an incentive high enough to move organic to our
12 area and suggest the Department remove the hauling costs
13 associated with organic milk from the northern San Joaquin
14 Valley to Sacramento haul to see if the 39.7 cent per
15 hundredweight is still a valid hauling cost. If it is
16 representative, we would like to have that information so
17 this issue can be addressed at the next transportation
18 allowance hearing.

19 Let me diverge a moment to make a request of the
20 Department. In the future, please make every effort to
21 have the hauling rate survey available well in advance of
22 the due date for alternative proposals. This information
23 is very important in analyzing the impact of hauling rate
24 changes and is often a necessary component of deciding
25 whether or not to file an alternative proposal. We

1 believe it is of sufficient importance that in the future
2 hearings be scheduled so as to allow the staff of the
3 Department adequate time to collect, prepare and
4 disseminate this critical information. For complex milk
5 movement issues a relatively minor delay would be
6 worthwhile in exchange for receiving current data upon
7 which to formulate proposals.

8 Moving back to today's proposals, Dr. Schiek
9 discussed in detail the situation that currently exists in
10 the Bay Area, Sonoma-Marín and Solano counties and
11 recommended a solution. Contained in the Dairy
12 Institute's proposal is the basic tenet that
13 transportation allowances should not be set so as to
14 afford one qualifying plant in the receiving area an
15 advantage over another.

16 Plants located in this, quote, Greater San
17 Francisco Bay Area, end quote, are all possible buyers of
18 milk from the Sonoma-Marín milk shed, thus requiring
19 careful analysis in setting transportation allowances that
20 do not favor one plant over another. We believe the
21 Department must give similar consideration to the
22 Sacramento deficit area.

23 We are specifically concerned about the impact of
24 DFA's proposal to increase transportation allowances for
25 milk moving into the Solano receiving area. In June, just

1 over 6 percent of the milk Crystal processed came from
2 dairies west of Sacramento. These dairies are considered
3 by CDFA to be located 18 constructive miles from our
4 plant.

5 A check of MapQuest indicated they were 22 miles
6 away from our D Street facility. Also according to
7 MapQuest, these same dairies are located 29 to 32 miles
8 from the fluid plant located in the Solano receiving area.
9 We are concerned that increasing the transportation
10 allowance into Solano will at some point cause this milk
11 to move away from Sacramento instead of toward it.
12 Currently these producers have a net haul of 24 cents per
13 hundredweight to come to Sacramento. That's 33 cents
14 minus the 9 cent transportation allowance. They received
15 15 cents -- they could receive 15 cents per hundredweight
16 to ship to Solano right now; and if DFA's proposal is
17 adopted, the transportation allowance would increase
18 another 3 cents to 18 cents per hundredweight.

19 We have a similar issue with milk located in the
20 Lodi area. As an example, a representative producer from
21 that area has been deemed to be 36 constructive miles from
22 Sacramento. MapQuest puts this dairy at 34 miles from our
23 D Street plant and 55 miles from the Solano receiving area
24 fluid plant. For delivering to Sacramento, this producer
25 receives a transportation allowance of 9 cents per

1 hundredweight, yielding a net haul rate of 24 cents per
2 hundredweight. The current transportation allowance to
3 Solano in the 45 to 99 mile bracket is 20 cents per
4 hundredweight; and under the DFA proposal, it will
5 increase to 28 cents per hundredweight.

6 Unfortunately the Department's hauling rate
7 survey does not include a haul from San Joaquin to Solano.
8 But the transportation allowance raised -- or with the
9 transportation allowance raised to 28 cents per
10 hundredweight, the haul rate could be as much as 52 cents
11 per hundredweight and this Lodi producer would simply be
12 ambivalent relative to which plant to serve.

13 By comparison, the northern San Joaquin Valley to
14 Bay Area and Solano County rate is reported at being 49.3
15 cents per hundredweight, which probably means it's less
16 costly to move milk out of the Lodi area than from further
17 south, thus indicating the likely consequence of DFA's
18 proposal will an incentive for milk located in Lodi to
19 move to Solano instead of into the Sacramento area.

20 We believe DFA's proposed transportation
21 allowance adjustments are undoubtedly designed to fix
22 certain problems that exist within their current supply
23 arrangements. I am confident their representatives will
24 present testimony and evidence which supports their
25 proposal. The Department should then give serious

1 consideration to what is presented. Our concern is over
2 the unintended consequences of any proposal, including
3 DFA's, that adversely impacts Crystal's ability to acquire
4 milk.

5 We feel the Department must use the detailed
6 information at their disposal to make changes in the
7 transportation allowance system that solve as many
8 problems as possible without causing new ones. The
9 industry can and certainly should voice their opinions,
10 but we do not have access to enough information to make
11 the best decisions on matters of transportation
12 allowances. That responsibility rests with the
13 Department.

14 Crystal has generally been comfortable in the
15 past with our ability to attract milk into the Sacramento
16 deficit area. Certainly transportation allowances have
17 played an integral role in providing that comfort by
18 reducing the net hauling rate to favorable levels for
19 producers who have chosen to supply our plants, and we
20 want to go on record today in support of maintaining the
21 overall system of transportation allowances.

22 With the exception of reverting back to
23 pre-pooling where a plant's ability to attract milk is
24 contingent upon their in-plant usage, transportation
25 allowances are the best method at the moment for moving

1 milk to higher usage plants. Perhaps the future will
2 bring something better and new, but for now we support
3 modifying the current system to best meet the needs of the
4 industry.

5 I do want to mention that at some point in the
6 not too distant future it is very likely the milk supply
7 in our traditional milk procurement area will no longer be
8 sufficient to meet our needs. The close in milk, so
9 contentious in past transportation allowance hearings,
10 continues to disappear.

11 In recent years we have lost five dairies located
12 within 15 constructive miles of our plants. And the one
13 remaining within this circle has his cows for sale or
14 perhaps sold right now. All of these dairies have gone
15 out of business due to urban development. Another four
16 dairies in the 15 to 20 mile zone have sold to developers
17 and we expect there will be more. In the southern
18 Sacramento county community of Galt, similar pressures are
19 occurring. We have another six dairies in that area who
20 are or will soon be facing the perils and pleasures of
21 urbanization.

22 Fortunately our remaining dairies have continued
23 to grow and keep our supply in relative balance with our
24 needs. We've also been able to purchase supplemental milk
25 from cooperatives in the area at reasonable prices. This

1 has kept milk in our plants at competitive prices thus
2 far, but the future is uncertain. As changes occur, we
3 will watch carefully our ability to procure milk. If it
4 seems sufficient milk is unavailable without subsidizing
5 the hauls, we would anticipate petitioning the Department
6 for adjustments in transportation allowances and perhaps
7 inclusion in the transportation credit system for bulk
8 movements of condensed skim.

9 That concludes my testimony. I appreciate being
10 able to express Crystal's views on these important
11 subjects.

12 I do request the opportunity to file a
13 post-hearing brief.

14 HEARING OFFICER ESTES: Your request is granted.

15 Are there panel questions at this time?

16 HEARING OFFICER ESTES: Apparently your testimony
17 is pretty clear and direct.

18 DAIRY MARKETING BRANCH ACTING CHIEF ERBA: I
19 have one.

20 HEARING OFFICER ESTES: Dr. Erba has one.

21 DAIRY MARKETING BRANCH ACTING CHIEF ERBA: Ms.
22 Hale, we've had a number of participants request changes
23 to the transportation allowance system and point very
24 heavily toward the increase to fuel costs.

25 How is it that your company has been able to

1 escape these increased fuel costs.

2 MS. HALE: We have had increases. However,
3 transportation allowances in our mind are set based on the
4 changing relationship between hauling to our plant and to
5 other opportunities. And because it appears that the rate
6 for those other opportunities have gone up consistent with
7 the haul rate to our plant, the actual relationship hasn't
8 changed.

9 And therefore there really is no justification
10 for making a change. We do have in our contracts -- the
11 producers' contracts for hauling, they do have an
12 escalator clause and it has been activated in this past
13 year, but it hasn't been changed since changed the rates
14 in May. And those new rates are included, I understand,
15 in the cost survey that was done.

16 DAIRY MARKETING BRANCH ACTING CHIEF ERBA: Okay.
17 Thank you.

18 HEARING OFFICER ESTES: Any additional questions?

19 All right. Thank you for your appearance today.

20 Are there any other witnesses at this time?

21 Seeing none.

22 The public hearing -- this public hearing is now
23 closed. For those of you who have requested the
24 opportunity to submit a post-hearing brief to the
25 Department, you may do so. But as we finally determined,

1 those briefs should be produced to the Department by 4:30
2 p.m., Monday, August the 16th, for consideration.

3 So again thank you for your appearance today.

4 And this aspect of the hearing is now closed.

5 (Thereupon the California Department of Food
6 and Agriculture public hearing adjourned
7 at 1:35 p.m.)

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1 CERTIFICATE OF REPORTER

2 I, JAMES F. PETERS, a Certified Shorthand
3 Reporter of the State of California, and Registered
4 Professional Reporter, do hereby certify:

5 That I am a disinterested person herein; that the
6 foregoing California Department of Food and Agriculture
7 hearing was reported in shorthand by me, James F. Peters,
8 a Certified Shorthand Reporter of the State of California,
9 and thereafter transcribed into typewriting.

10 I further certify that I am not of counsel or
11 attorney for any of the parties to said hearing nor in any
12 way interested in the outcome of said hearing.

13 IN WITNESS WHEREOF, I have hereunto set my hand
14 this 13th day of August, 2004.

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22 JAMES F. PETERS, CSR, RPR
23 Certified Shorthand Reporter
24 License No. 10063
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